

PFE ORIGINAL

Q1-88-014

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1 of 126

1. Sale and Purchase of Shares

Industries does hereby sell, convey, transfer, assign, and set over unto Lime Ridge and Lime Ridge does hereby purchase from Industries, 1,164,136 shares of the issued and outstanding shares of capital stock of Safety Light (such shares hereinafter collectively being referred to as the "Shares"), which Shares constitute all of the issued and outstanding shares of capital stock of Safety Light.

2. Purchase Price

2.1. The purchase price to be paid by Lime Ridge to Industries for the Shares is Three Hundred Fifty Thousand (\$350,000) Dollars.

2.2. Payment of the total purchase price for the Shares is being made by Lime Ridge as follows:

(a) Concurrently herewith, Lime Ridge is paying to Industries, by good bank or certified check, the sum of Thirty Five Thousand (\$35,000) Dollars, receipt of which is hereby acknowledged by Industries.

(b) The balance of the purchase price of Three Hundred Fifteen Thousand (\$315,000) Dollars shall be paid by Lime Ridge to Industries pursuant to the terms of a negotiable promis-

sory note ("Promissory Note"), in the form of Exhibit A hereto, which is concurrently herewith being executed and delivered by Lime Ridge to Industries.

2.3. Nothing contained herein shall be deemed to impose any personal liability on the shareholders of Lime Ridge for the payment of the balance of the purchase price owing to Industries pursuant to the Promissory Note. The shareholders of Lime Ridge shall, however, use their best efforts as officers, shareholders and directors of Lime Ridge to cause it to make all payments required under the Promissory Note and to comply with and fulfill the obligations imposed herein upon Lime Ridge and in any other document, agreement or instrument executed by Lime Ridge in connection with the transactions contemplated hereby.

3. Collateral Security; Merger

3.1. As collateral security for Lime Ridge's obligations to Industries under the Promissory Note:

(a) Lime Ridge is granting to Industries a security interest in the Shares by pledging the same pursuant to a Pledge and Escrow Agreement which is concurrently herewith being executed and delivered by Lime Ridge. A copy of the Pledge and Escrow Agreement is attached hereto as Exhibit B.

(b) Safety Light is, concurrently with the execution hereof, guaranteeing Lime Ridge's obligations to Industries under the Promissory Note, by executing and delivering to Industries a Guaranty of Payment, a copy of which is attached hereto as Exhibit C, and is securing its obligations to guarantee by granting to Industries a security interest in the Collateral more particularly described in the Security Agreement which is, concurrently herewith, being executed and delivered by Safety Light to Industries, a copy of which Security Agreement is attached hereto as Exhibit D.

(c) Lime Ridge is securing its obligations under the Promissory Note by granting to Industries a security interest in the Collateral more particularly described in the Security Agreement which is, concurrently herewith, being executed and delivered to by Lime Ridge to Industries, a copy of which is attached hereto as Exhibit D.

3.2. Lime Ridge agrees that it will, within ninety (90) days from the date hereof, merge Lime Ridge into Safety Light, with Safety Light being the surviving corporation. Upon the effecting of the aforesaid merger, and as provided for in the Pledge and Escrow Agreement, the Shares pledged by Lime Ridge to Industries shall (if there be no default at such time under the

Promissory Note) be released from escrow, and returned to Lime Ridge.

4. Warranties and Representations of Industries

Industries hereby warrants and represents to Lime Ridge knowing and intending that it is relying hereon in entering into the transactions contemplated hereby that:

4.1. (a) Industries is a corporation duly organized, validly existing and in good standing under the laws of the State of Delaware.

(b) Safety Light is a corporation duly organized, validly existing and in good standing the the laws of the State of Delaware; and has full corporate power to carry on its business as now conducted and to own and operate the properties and assets now owned and operated by it.

4.2. (a) The authorized capital stock of Safety Light consists of 3,500,000 shares of Common stock, 1,164,136 shares of which have heretofore been issued. The issued and outstanding shares of capital stock of Safety Light have been validly issued and are fully paid and non-assessable.

(b) Industries owns all of the issued and outstanding shares of capital stock of Safety Light.

4.3. (a) Safety Light owns all of the issued and outstanding shares of capital stock of Metreal Corporation, a Pennsylvania corporation ("Metreal"), all of which shares ("Metreal Shares") have been validly issued and are fully paid and non-assessable.

(b) Metreal is a corporation duly organized, validly existing and in good standing the the laws of Pennsylvania and has full corporate power to carry on its business as now conducted and to own and operate the properties and assets now owned and operated by it.

4.4. The execution of this Agreement and the consummation of the transactions contemplated hereby do not and will not violate Industries' or Safety Light's Certificates of Incorporation, By-laws or governing documents, or any material indenture or agreement to which either of them is a party or by which either of their properties or assets are bound.

4.5. Except as indicated on Schedule A hereto, there are no actions, suits, proceedings, or investigations pending

against Safety Light or Metreal or any of their properties or assets, at law or in equity, before or by any federal, state, municipal or other governmental court, department, commission, agency or instrumentality, domestic or foreign.

4.6. Industries owns the Shares free and clear of all liens, security interests, encumbrances and claims of third parties and has the absolute and unrestricted right to sell, transfer and assign the same to Lime Ridge pursuant to the terms hereof. No person or entity has any option, call, claim or other right with respect to the Shares, or any other shares of capital stock of Safety Light.

4.7. Safety Light owns the Metreal Shares free and clear of liens, encumbrances, security interests and claims of third parties. No person or entity has any option, call, claim or other right with respect to the shares of capital stock of Metreal.

4.8. Except as described in Schedule B hereto, neither Safety Light nor Metreal is a party to nor bound by any oral or written: (i) employee collective bargaining agreement, employment agreement (other than employment agreements under which

REC

Safety Light's or Metreal's sole obligation is to make current wage or salary payments, which obligation is terminable by them without premium or penalty on notice of ninety (90) days or less), consulting agreement, deferred compensation agreement, or covenant not to compete; (ii) contractual agreement with any employee or agent; (iii) contracts or commitments providing for payments based upon sales, purchases or profits; (iv) power of attorney; or (v) employee's pension, profit-sharing, stock option, bonus, incentive, stock purchase, welfare, life insurance, hospital and medical benefit plan or any other employment benefit agreement.

4.9. Schedule C hereto contains a materially complete and accurate list of each contract to which Safety Light or Metreal is a party which (i) requires either of them to pay an aggregate of more than Ten Thousand (\$10,000) Dollars during the life of the contract; or (ii) requires either of them to render services for more than twelve (12) months after the date of this Agreement.

4.10. Schedule D hereto contains a materially complete and accurate list as of the date of this Agreement, of the name of each bank in which Safety Light or Metreal maintains an ac-

REC

count or safety deposit box, and the names of all persons authorized to draw thereon or to have access thereto.

4.11. (a) Schedule E hereto contains a materially complete and accurate list of all machinery, equipment, and other tangible personal property (excluding inventory) owned or leased by Safety Light or Metreal, all such leased property being so indicated.

(b) Except as set forth on Schedule E hereto, Safety Light and/or Metreal, as the case may be, has good and marketable title to all of its property, and owns the same free and clear of all liens, security interests, encumbrances and claims of third parties.

4.12. Safety Light and Metreal have filed all federal, state, and local tax returns which are required to be filed prior to the date hereof, and all taxes shown thereon have been paid when due.

4.13. (a) Schedule F hereto contains a materially complete list or description of: (1) all United States and foreign patents, patent applications, copyright, copyright registrations, all United States, state and foreign trade names, trademarks and

service mark registrations and applications and all other trade names, trademarks and service marks owned by Safety Light and/or Metreal and shows in each case, the product, device, process, service, business or publication covered thereby, the registered owner, expiration date and number, if any; (ii) description of all licenses and other agreements relating to the assets, property or rights described in the preceding clause to which Safety Light or Metreal is a party, showing in each case the parties and the material terms; and (iii) a description of all licenses or agreements pertaining to know-how, trade secrets, inventions, disclosures, or uses of ideas and industrial property to which Safety Light or Metreal is a party, showing in each case the properties and material terms.

(b) No proceedings are pending which challenges the validity or ownership of any patent, trademark, service mark, copyright, or the ownership of any other right or property described in the preceding sentence

5. Warranties and Representations of Lime Ridge

Lime Ridge hereby warrants and represents to Industries, knowing and intending that Industries is relying hereon in entering into the transactions contemplated hereby that:

5.1. It is a corporation duly organized, validly existing and in good standing under the laws of the Commonwealth of Pennsylvania.

5.2. It has the corporate power and authority to execute and perform this Agreement, and any other agreements, documents, and/or instruments contemplated hereby.

5.3. The execution of this Agreement and the consummation of the transactions contemplated hereby do not violate its Certificate of Incorporation, By-laws, governing documents or any other material indenture or agreement to which it is a party or by which its properties or assets are bound.

5.4. This Agreement, and any other agreement, document and/or instrument to be executed by it in connection with the transactions contemplated hereby, constitute the valid and binding agreements of Lime Ridge, enforceable in accordance with their respective terms

5.5. Except as specifically set forth in this Agreement, Industries has not made any warranty, representation or promise whatsoever regarding the subject matter of this Agreement, the financial condition of Safety Light or Metreal or the

value of their assets or properties.

6. No Brokers

The parties hereto represent and warrant to each other that neither they nor any agent or affiliated company has employed any broker or finder in connection with this Agreement and the transactions contemplated hereby, and agree to indemnify and hold the other harmless from any and all liabilities (including without limitation, reasonable attorney's fees and disbursements paid or incurred in connection with such liabilities) or brokerage commissions or finders fees in connection with this Agreement or the transactions contemplated hereby, insofar as such claims shall be based upon arrangements or agreements or actions made or alleged to have been made by or on behalf of such party. This obligation to indemnify shall survive the Closing

7. Other Concurrent Action

Concurrently herewith the following is also transpiring:

(a) Industries is delivering to Lime Ridge a certified copy of the resolution of its Board of Directors authorizing the execution by it of this Agreement and the consummation of the transactions contemplated hereby;

(b) Lime Ridge is delivering to Industries a cer-

ified copy of the resolution of Lime Ridge's Board of Directors authorizing the execution by it of this Agreement and the consummation of the transactions contemplated hereby;

(c) Safety Light and Lime Ridge, are pursuant to the Security Agreement, executing and delivering to Industries appropriate UCC-1 Financing Statements to perfect the security interest granted to Industries in the Collateral;

(d) Safety Light and Metreal, as landlord, and USR Metals, Inc., as tenant, are entering into a lease, a copy of which is attached hereto as Exhibit E.

(e) Industries is delivering to Lime Ridge, Safety Light Stock Certificate No. | , evidencing the Shares, duly endorsed for transfer.

8. No Implied Warranties

It is expressly acknowledged by Lime Ridge that Industries has and hereby disclaims any and all implied and express warranties respecting the physical condition of the tangible personal property of Safety Light and Metreal and their suitability to any particular use. The implied warranties which are hereby disclaimed by Industries include without limitation, merchantability and fitness for a particular purpose. It is also expressly acknowledged by Lime Ridge that Industries has not and

does not make any warranties or representations respecting the real estate owned or leased by Safety Light and/or Metreal, including, without limitation, warranties and representations respecting its physical condition and its ability to be used for any particular purpose or purposes.

9. Orange Litigation

9.1. (a) Reference is hereby made to that certain action entitled "T & E Industries, Inc , a New Jersey corporation, Plaintiff vs. United States Radium Corporation, a Delaware Corporation, Defendant", Superior Court of New Jersey, Law Division: Essex County, Docket No : L-41346-80 (the aforesaid action is hereinafter referred to as the "Orange Litigation").

(b) The term "Related Litigation", as used in this Section 9 shall mean any suit, proceeding, claim, etc. made or instituted against Industries, Lime Ridge, Safety Light or any Affiliates of Industries (as hereinafter defined) if such suit, proceeding or claim arises out of the facts and circumstances giving rise to the Orange Litigation.

9.2. (a) Immediately after the date hereof, Lime Ridge shall cause Safety Light to substitute new counsel ("New Counsel") for the counsel presently representing Safety Light in the Orange Litigation ("Old Counsel").

720

(b) Industries shall cause Old Counsel, on the request of Lime Ridge (and provided that Old Counsel is not prohibited from so doing by reason of the existence of a conflict) to consult with and cooperate with New Counsel in the defense of the Orange Litigation.

(c) Lime Ridge and Safety Light shall be fully responsible for the payment of all legal fees and related out-of-pocket disbursements and expenses incurred by New Counsel in the defense of the Orange Litigation. Lime Ridge agrees that it will and will cause Safety Light to vigorously defend the Orange Litigation or any Related Litigation.

(d) Industries shall be fully responsible for the payment of all legal fees and related out-of-pocket disbursements and expenses incurred by it in connection with Old Counsel's cooperating and consulting with New Counsel in the defense of the Orange Litigation.

9.3. (a) (i) Lime Ridge agrees that it will not and will not permit or allow Safety Light to settle the Orange Litigation or any Related Litigation without the prior written consent of Industries; provided, however, that the prior written consent of Industries need not be obtained if any settlement entered into by Safety Light or Lime Ridge requires only the payment of a sum certain, which sum certain is paid by Safety

Light or Lime Ridge at the consummation of the settlement.

(ii) Except in the limited circumstance described in Section 9.3(b) below Lime Ridge and Safety Light shall indemnify and hold Industries and its Affiliates harmless from and against any and all liabilities, losses, costs, damages, demands, judgments, suits, legal fees and out-of-pocket expenses incurred, imposed or suffered by Industries and/or its Affiliates in connection with, resulting from or relating to the Orange Litigation, the Related Litigation or claims therein. The obligation to indemnify shall survive the execution and delivery of this Agreement and the consummation of the transactions contemplated hereby. The term "Affiliates" as used herein shall mean any corporation or entity that directly or indirectly through one or more of its intermediaries, controls or is controlled by or is under common control with, Industries

(b) Lime Ridge shall and agrees to cause Safety Light to advise and inform Industries of any settlement offers or proposals made by the plaintiff in the Orange Litigation, or in any Related Litigation. If Industries requests that Safety Light or Lime Ridge accept any proposed settlement offer, Lime Ridge shall and agrees to cause Safety Light to accept such settlement. If Lime Ridge and/or Safety Light would not accept such proposed settlement offer except for the insistence of Industries pursuant to the terms hereof, then Industries agrees to con-

tribute to Safety Light twenty-five (25%) per cent of the amount required to be paid by Safety Light pursuant to the agreed-upon settlement.

10. California Litigation

10.1. Reference is hereby made to that certain action entitled "Penteco, a partnership, Plaintiff, vs. United States Radium Corporation, a Delaware corporation, Defendant", United States District Court, Central District, California (the afore-said action is hereinafter referred to as the "California Litigation").

10.2. Lime Ridge agrees that Industries shall have the continuing and irrevocable right to designate the attorneys representing Safety Light in the California Litigation

10.3. Industries agrees to pay and be fully responsible for payment of all legal fees and related out-of-pocket disbursements and expenses incurred by Safety Light in defending the California Litigation.

10.4. Lime Ridge agrees that it will not allow or permit Safety Light to compromise, settle, or consent to the entry of a judgment with respect to the California Litigation, without first obtaining the prior written consent of Industries.

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10.5. Industries agrees to contribute to Safety Light a sum, up to a maximum of \$100,000, in connection with any judgment entered against Safety Light in the California Litigation, or in connection with any settlement of the California Litigation, provided that Industries has consented to such settlement.

10.6. Except to the extent that Industries is obligated to contribute in accordance with Section 10.5 hereof, Lime Ridge shall indemnify and hold Industries and its Affiliates harmless from and against any and all liabilities, losses, costs, damages, demands, judgments, suits, legal fees and out-of-pocket expenses incurred, imposed or suffered by Industries and/or its Affiliates in connection with, resulting from or relating to the California Litigation or claims therein. The obligation to indemnify shall survive the execution and delivery of this Agreement and the consummation of the transactions contemplated hereby. The term "Affiliates" as used herein shall mean any corporation or entity that directly or indirectly through one or more of its intermediaries, controls or is controlled by or is under common control with, Industries.

11. Tax Allocation

Lime Ridge hereby agrees to cause Safety Light to pay to Industries its "share of Industries' consolidated tax liability" as that term is hereinafter defined. Safety Light's

P2C

"share of Industries' consolidated tax liability" is defined as the dollar amount resulting from multiplying (i) Safety Lights taxable income for Federal income tax purposes for the period January 1, 1982 to the date hereof, by (ii) Forty-Six (46) per cent. Such payment shall be due within 90 days from the date hereof.

12. Miscellaneous

12.1. This Agreement represents the entire understanding of the parties hereto with respect to the subject matter hereof, and supersedes any and all prior and contemporaneous negotiations, understandings or agreements, whether verbal or written, all of which prior and contemporaneous negotiations, understandings and agreements are hereby rendered null and void

12.2. This Agreement shall be binding upon and shall inure to the benefit of the parties hereto and their respective successors and assigns.

12.3. This Agreement shall be governed by and shall be construed in accordance with the laws of the Commonwealth of Pennsylvania.

12.4. No press release, public announcement or other communication relating to the transactions described herein shall

be made or issued by or on behalf of either party, without the prior written approval of the other, which shall not be unreasonably withheld.

12.5. Lime Ridge agrees that it will do all which is necessary to change the name of the corporation surviving the merger of Lime Ridge into Safety Light to "Safety Light Corporation".

12.6. In 1980, Industries and its Affiliates were reorganized pursuant to a Plan of Reorganization submitted to and approved by Industries' shareholders at a meeting held in August, 1980. In connection therewith, various of the assets of United States Radium Corporation were allocated along divisional lines to newly formed subsidiaries of Industries. Lime Ridge acknowledges that the only assets and properties of Safety Light (excluding inventory and accounts receivable) are as listed on Schedule E hereto. Lime Ridge agrees that it will, from time to time, upon the request of Industries, take such action and execute such instruments as is necessary to establish the ownership of property other than that property listed on Schedule E hereto.

IN WITNESS WHEREOF, the parties hereto have executed this Agreement by their duly authorized corporate officers the

day and year first above written.

ATTEST:

USR INDUSTRIES, INC.

By _____

By _____

Robert T. McElvany

ATTEST:

LIME RIDGE INDUSTRIES, INC

By _____

By _____

David John Watts

John T. Miller

DAVID JOHN WATTS, Vice President

JOHN T. MILLER, President

PROMISSORY NOTE

PRINCIPAL AMOUNT: \$315,000

DATE: May 24, 1982

FOR VALUE RECEIVED, LIME RIDGE INDUSTRIES, INC., a Pennsylvania corporation ("Maker"), promises to pay to the order of USR INDUSTRIES, INC., a Delaware corporation ("Holder") at Suite 217, 2203 Timberloch Place, The Woodlands, Texas 77380 or at such other place as the Holder hereof may from time to time designate in writing, the principal sum of Three Hundred Fifteen Thousand (\$315,000) Dollars, with interest thereon from the date hereof at the rate of eight (8%) per cent per annum in lawful money of the United States, which shall be paid in the following manner:

The principal balance hereof shall be payable in thirty-four (34) installments of principal, in the amounts and on the dates set forth in Schedule A hereto. Each payment of principal shall be accompanied by payment of accrued but unpaid interest on the unpaid principal balance as of the date of each principal payment.

The entire unpaid balance of principal, together with accrued but unpaid interest thereon shall be due and payable on December 31, 1990.

Exhibit A

XXIX-0019

Ex. 9
62 of 126

Each payment made hereunder shall be applied first on account of interest and the balance, if any, to the reduction of principal.

As security for the payment of the monies owing hereunder, the Maker has executed and delivered to the Holder a Pledge and Escrow Agreement, of this date, respecting the Pledged Shares (as defined therein). The terms and provisions of the Pledge and Escrow Agreement are incorporated herein by reference as if expressly set forth.

As further security for the payment of the monies owing hereunder, Safety Light Corporation and Maker have executed and delivered to the Holder a Security Agreement, of this date, respecting the Collateral (as defined therein). The terms and provisions of the Security Agreement are incorporated herein by reference as if expressly set forth.

The full amount of the principal balance owing, and the accrued but unpaid interest thereon, shall, at the election of the Holder hereof, become immediately due and payable upon the occurrence of any of the following ("Events of Default").

(a) the failure of the Maker to pay any

installment of principal or interest or late charge if not paid within fifteen (15) days of the date when the same is due and payable;

(b) the failure of the Maker to perform or observe any term, provision, covenant or agreement contained in this Note, or the Pledge and Escrow Agreement, or the failure of the Maker to perform or observe any term, covenant, condition, condition, stipulation provision, obligation, warranty or representation contained in or imposed upon Maker pursuant to that certain Stock Purchase Agreement, of this date, entered into among Maker and Holder;

(c) the sale of all or substantially all of the assets of Maker;

(d) the failure of Safety Light Corporation or the Maker to perform or observe any term, covenant, condition, stipulation, provision, obligation, warranty or representation contained in or imposed upon either of them pursuant to the Security Agreement.

If the Holder shall, upon the occurrence of an Event of Default, place this Note in the hands of an attorney for collection, the Holder shall be entitled to receive from the Maker reasonable attorney's fees, costs of suit, and out-of-pocket disbursements incurred in connection therewith.

The Maker shall pay to Holder, upon demand, a charge of four (4%) per cent of any amount payable (including principal and interest) by the terms of this Note which are not paid within fifteen (15) days of the date the same shall become due and payable.

The Maker and all endorsers and guarantors of this Note, waive presentment, demand for payment, protest, and notice of dishonor of this Note, authorize the Holder without notice or further consent, to grant an extension of time for the payment of any monies owing under this Note, and to waive compliance with any provisions of this Note.

The provisions of this Note are severable, and the invalidity or unenforceability of any provision shall not alter or impair the remaining provisions of this Note.

This Note shall be construed under and governed by the laws of the Commonwealth of Pennsylvania.

Whenever used herein, the term "Maker" and "Holder" shall be deemed to include their respective heirs, executors, administrators, successors and assigns.

IN WITNESS WHEREOF, Lime Ridge Industries, Inc. has executed this Note by its duly authorized corporate officers the day and year first above written.

ATTEST:

LIME RIDGE INDUSTRIES, INC.

By /s/ DAVID JOHN WATTS

DAVID JOHN WATTS, Vice President

By /s/ JOHN T. MILLER

JOHN T. MILLER, President

PLEDGE AND ESCROW AGREEMENT

This Agreement is made this 24th day of May, 1982, among LIME RIDGE INDUSTRIES, INC., a Pennsylvania corporation, having an address at 4150A Old Berwick Road, Bloomsburg, Pennsylvania ("Lime Ridge"); USR INDUSTRIES, INC., a Delaware corporation, having an address at Suite 217, 2203 Timberloch Place, The Woodlands, Texas 77380 ("Industries"); and HANNOCH, WEISMAN, STERN, BESSER, BERKOWITZ & KINNEY, P. A., having offices at 744 Broad Street, Newark, New Jersey ("Escrow Agent").

RECITALS:

A. Concurrently with the execution hereof, the following has transpired:

(i) Industries has sold to Lime Ridge, pursuant to the terms of a Stock Purchase Agreement, of this date, all of the issued and outstanding shares of capital stock of Safety Light Corporation, a Delaware corporation ("Safety Light"); and

(ii) Lime Ridge has executed and delivered to Industries its promissory note ("Note") in the principal sum of Three Hundred Fifteen Thousand (\$315,000) Dollars, which Note evidences Lime Ridge's obligation to pay the deferred purchase

Exhibit B

XXIX-001R

Ex. 9
67 of 126

price for the aforementioned shares.

B. Industries would be unwilling to consummate the transactions more particularly described in the Stock Purchase Agreement unless Lime Ridge secures its obligations to pay the indebtedness evidenced by the Note by pledging the shares of capital stock of Safety Light purchased from Industries.

NOW, THEREFORE, in consideration of the Recitals and the mutual covenants herein contained, the parties hereto agree as follows:

1. Pledge of Shares

1.1. As collateral security for (i) the due and punctual payment of the Note and any and all increases, extensions, renewals, substitutions and changes in the form thereof; (ii) the full, prompt and unconditional performance of all obligations, covenants, warranties, representations, promises and liabilities of Lime Ridge pursuant to the Stock Purchase Agreement, Note, this Agreement and any other agreement executed and/or delivered by Lime Ridge in connection with the transactions contemplated by the Stock Purchase Agreement; and (iii) all costs and expenses incurred and/or paid by Industries in enforc-

ing its rights pursuant to the Stock Purchase Agreement, Note and this Agreement, Lime Ridge hereby pledges and grants to Industries a security interest in the One Million One Hundred Sixty Four Thousand One Hundred Thirty-Six (1,164,136) shares of the issued and outstanding shares of capital stock of Safety Light owned by it ("Pledged Shares").

1.2. Concurrently with the execution hereof, Lime Ridge has delivered to the Escrow Agent, Safety Light stock certificate No. , evidencing the Pledged Shares, together with a stock assignment executed in blank.

1.3. The Escrow Agent acknowledges receipt of the Pledged Shares and the blank stock assignment and agrees to hold the same in escrow, subject to and upon the terms and conditions of this Agreement, and to carry out the provisions of this Agreement on its part to be performed.

1.4. (a) Any shares issued on or exchanged for the Pledged Shares as a result of any stock dividends, stock splits, subdivisions, combinations, reclassifications, reorganizations, mergers, consolidations, exercise of warrants or options, or similar transactions respecting the Pledged Shares shall become

part of the Pledged Shares and shall be held on the same terms as the shares on or in exchange for which such shares have been issued.

(b) So long as an Event of Default (as defined in the Note) has not occurred under the Note, Lime Ridge shall have the right to vote the Pledged Shares and to give consents and ratifications with respect thereto.

1.5. (a) If an Event of Default under the Note shall occur and Industries desires to exercise its rights in and to the Pledged Shares as secured party, then Industries shall give written notice ("Default Notice") to the Escrow Agent and Lime Ridge, stating that an Event of Default has occurred and requesting the Escrow Agent to deliver the Pledged Shares to Industries.

(b) If within twenty (20) days after the giving of the Default Notice, Lime Ridge has not objected to delivery of the Pledged Shares to Industries by written notice ("Objection Notice") given to the Escrow Agent and to Industries, then the Escrow Agent, without further instructions from any party hereto, shall deliver to Industries the Pledged Shares and the stock assignment delivered to the Escrow Agent.

(c) If the Escrow Agent shall receive an Objection

Notice from Lime Ridge within such twenty (20) day period, then the Escrow Agent shall retain the Pledged Shares until it shall receive any of the following:

(i) written instructions signed by Industries and Lime Ridge setting forth to whom the Pledged Shares shall be delivered; or

(ii) a final order of a court of competent jurisdiction setting forth to whom the Pledged Shares shall be delivered.

1.6 (a) If Lime Ridge has made all payments required under the Note to Industries, and Lime Ridge requests the Escrow Agent deliver to it the Pledged Shares, the Escrow Agent, without any obligation to determine whether all the required payments under the Note have been made, shall notify Industries that it is prepared to deliver the Pledged Shares to Lime Ridge. If Industries objects to such delivery, it shall give written notice to the Escrow Agent and Lime Ridge within twenty (20) days after receiving the notice of the Escrow Agent.

(b) If the Escrow Agent does not receive any notice from Industries within said twenty (20) day period objecting to the release of the Pledged Shares, the Escrow Agent shall, without further instructions, deliver the Pledged Shares to Lime

Ridge.

(c) If the Escrow Agent receives such notice of objection from Industries within such twenty (20) day period, the Escrow Agent shall retain the Pledged Shares until it shall receive any of the following:

(i) written instructions signed by Industries and Lime Ridge setting forth to whom the Pledged Shares shall be delivered; or

(ii) a final order of a court of competent jurisdiction setting forth to whom the Pledged Shares shall be delivered.

2. Warranties and Representations by Lime Ridge.

Lime Ridge hereby warrants and represents to Industries, knowing and intending that it is relying hereon in entering into the transactions contemplated by the Stock Purchase Agreement that:

2.1. Lime Ridge owns the Pledged Shares free and clear of all liens, encumbrances, security interests and claims of third parties. The Pledged Shares have been fully paid for and are non-assessable.

2.2. The Pledged Shares are not subject to any restrictions respecting their transferability or other disposition. Lime Ridge is not a party to nor bound by any shareholders' agreement, buy-sell agreement or other agreement or arrangement restricting its ability to transfer or dispose of the Pledged Shares.

2.3. Lime Ridge has full voting rights with respect to the Pledged Shares. The Pledged Shares are not subject to any voting agreement, proxy, voting trust or other arrangement whereby its voting rights to the Pledged Shares have been restricted or transferred.

2.4. There are no existing options, warrants, calls or commitments of any character relating to the Pledged Shares.

2.5. The execution, delivery and performance by it of this Agreement and the consummation of the transactions contemplated hereby have been duly authorized by all requisite corporate action; are not inconsistent with and will not violate its Certificate of Incorporation, By-laws or other governing documents; and does not, and will not, contravene any provisions of

or constitute a default under any contract, instrument or agreement to which it is a party or by which its properties or assets are bound.

3. Covenants by Lime Ridge

Lime Ridge hereby covenants that until the Note is paid in full that:

3.1. It will not consolidate or merge with another entity, except for the merger of Lime Ridge into Safety Light.

3.2. It will not allow or permit Safety Light to issue any shares of its capital stock or securities convertible into shares of its capital stock.

4. Remedies of Industries

4.1. (a) From and after the occurrence of an Event of Default under the Note, and the delivery of the Pledged Shares to Industries pursuant to the terms hereof, Industries shall have the right to:

(i) vote any or all of the Pledged Shares, and give all consents, waivers and ratifications with respect thereto and otherwise act in all matters with respect thereto as the outright owner thereof (Lime Ridge hereby irrevoc-

ably constituting and appointing Industries as its proxy and attorney in fact with full power of substitution so to do, and Lime Ridge hereby agreeing to execute at any time in the future such additional instrument or instruments to confirm the proxy and power hereby granted);

(ii) receive all dividends and all other distributions of any kind on the Pledged Shares;

(iii) exercise any and all rights of conversion or exchange, and any and all other rights, privileges, options or powers of the owner of the Pledged Shares pertaining or relating thereto (Lime Ridge hereby irrevocably constituting and appointing Industries its proxy and attorney in fact with full power of substitution so to do, and Lime Ridge hereby agreeing to execute at any time in the future such additional instrument or instruments to confirm the power hereby granted); and

(iv) from time to time, without advertisement or right of redemption by Lime Ridge, at its option, to sell, re-sell, assign, transfer and deliver all or any part of the Pledged Shares at any broker's board or exchange or at public or private sale, for cash or on credit, or for future delivery, and in connection therewith, to grant options and impose reasonable conditions such as requiring any purchaser to represent that any stock constituting any part of the Pledged Shares is being purchased for investment purposes only. Upon each such sale,

Industries may purchase all or any part of the Pledged Shares being sold free from and discharged of all trusts, claims, rights of redemption and equities of Lime Ridge. At any such sale of the Pledged Shares, Industries shall have the right to make payment of any amount bid by it by setting off against such bid all or any part of the amount then due to Industries under the Note. Lime Ridge agrees that a notice sent at least five (5) days before the date of an intended sale or the date after which any private sale or other intended disposition of the Pledged Shares is to be made, shall be deemed to be commercially reasonable notice of such sale or disposition.

4.2. Industries, in addition to any other rights granted to it hereunder, and at law, shall be entitled to all rights and remedies of a secured party under the Uniform Commercial Code, as adopted by the Commonwealth of Pennsylvania.

4.3. The proceeds, if any, of any sale by Industries of the Pledged Shares shall be applied as follows: First, to the payment of all fees and expenses incurred by Industries in selling or disposing of the Pledged Shares, including but not limited to legal fees and expenses; Second, to pay the indebtedness secured hereby; and Third, to pay any excess

remaining to Lime Ridge.

5. Escrow Agreement

5.1. The parties to this Agreement, other than the Escrow Agent, acknowledge and agree that the Escrow Agent:

(a) is not a party to, and is not bound by any agreement referred to herein or by any agreement among the other parties hereto or their respective heirs, administrators, successors or assigns, other than as herein set forth.

(b) is acting hereunder as a depositary only and is not responsible or liable in any manner for the sufficiency, genuineness or validity of any instrument deposited with it, or for the form of execution of such instrument, or for the identity, authority, or rights of any person executing or depositing it.

(c) shall be protected in acting upon any written notice, request, waiver, consent, receipt or other papers or documents believed by it to be genuine and to have been made, signed, sent or presented by the proper party or parties.

(d) shall not be liable for any error of judgment or for any act done or step taken by it in good faith, or for any mistake of law, or for anything which it may do or refrain from doing in connection herewith, except its own will-

full misconduct.

(e) may consult with legal counsel in the event of any disputed question as to the construction of any provision hereof, or its duties hereunder, and shall incur no liability and shall be fully protected in acting in accordance with the opinion and instructions of such counsel.

5.2. The parties hereto acknowledge that the Escrow Agent may be serving as counsel to Industries in connection with the transactions contemplated hereby and may continue to serve as its counsel. The Escrow Agent is merely acting as a stakeholder hereunder and the parties agree that the Escrow Agent may continue to serve as Industries' counsel in connection with any dispute or controversy arising out of this Agreement or the transactions contemplated hereby.

5.3. The Escrow Agent shall be indemnified and held harmless, and reimbursed by the parties hereto for all expenses, claims and obligations incurred by it pertaining to its duties hereunder. The obligation of the parties hereto to indemnify, hold harmless and reimburse the Escrow Agent shall be joint and several.

6. Merger of Lime Ridge with Safety Light

6.1. Notwithstanding anything to the contrary contained in this Agreement, Lime Ridge shall be entitled to have the Pledged Shares released to it upon the finalization of the merger of Lime Ridge into Safety Light (if there does not exist, at such time, an Event of Default under the Note, or an event which, with the giving of notice or passage of time, or both, would become an Event of Default). If Lime Ridge has merged itself into Safety Light and desires that the Pledged Shares be released to it, it shall give written notice to the Escrow Agent and to Industries, requesting that the Pledged Shares be released to it, said notice to state that the aforesaid merger has been effectuated and said notice to be accompanied by evidence of the effectuation of said merger.

6.2. If within twenty (20) days after the giving of the aforesaid notice, Industries has not objected to the delivery of the Pledged Shares to Lime Ridge by written notice given to the Escrow Agent and to Lime Ridge, then the Escrow Agent, without further instructions from any party hereto, shall deliver to Lime Ridge the Pledged Shares and stock assignment delivered to the Escrow Agent.

6.3. If the Escrow Agent shall receive an objection notice from Industries within such twenty (20) day period,

then the Escrow Agent shall retain the Pledged Shares until it has received any of the following:

(i) written instructions signed by Industries and Lime Ridge setting forth to whom the Pledged Shares shall be delivered; or

(ii) a final order of a court of competent jurisdiction setting forth to whom the Pledged Shares shall be delivered.

7. Miscellaneous

7.1. This Agreement represents the entire understanding of the parties hereto with respect to the subject matter hereof and supersedes any and all other prior negotiations or agreements which are hereby rendered null and void. This Agreement may not be amended or modified except by a writing executed by all of the parties hereto.

7.2. This Agreement shall be governed by and shall be construed in accordance with the laws of the Commonwealth of Pennsylvania.

7.3. This Agreement shall be binding upon and shall inure to the benefit of the parties hereto, and their respective heirs, successors, administrators, executors and assigns.

7.4. Paragraph headings contained in this Agreement are for convenience of reference only and shall not be deemed a part of this Agreement.

7.5. All notices required to be given hereunder shall be given by certified mail, return receipt requested, addressed to the parties at their addresses above written, or at such other address as may be given by such party by like notice.

IN WITNESS WHEREOF the parties hereto have executed this Agreement the day and year first above written.

ATTEST:

J. H. Seltman

USR INDUSTRIES, INC.

By *Robert T. McElreath*

ATTEST:

David John Watts
DAVID JOHN WATTS, Vice President

LIME RIDGE INDUSTRIES, INC.

By *John T. Miller*
JOHN T. MILLER, President

HANNOCH, WEISMAN, STERN, BESSER,
BERKOWITZ & KINNEY, P.A.

By _____

GUARANTY OF PAYMENT

This Guaranty is made this 24th day of May, 1982, by SAFETY LIGHT CORPORATION, a Delaware corporation having an address at 4150 A Old Berwick Road, Bloomsburg, Pennsylvania ("Guarantor"), to USR INDUSTRIES, INC., a Delaware corporation having an address at Suite 217, 2203 Timberloch Place, The Woodlands, Texas 77380 ("Industries").

RECITALS:

A. Concurrently with the execution hereof the following has transpired:

(i) Industries has, pursuant to the terms of a Stock Purchase Agreement, of this date, sold to Lime Ridge Industries, Inc. ("Lime Ridge") all of the issued and outstanding shares of capital stock of Safety Light;

(ii) Lime Ridge has executed and delivered to Industries a promissory note ("Note"), of this date, in the principal sum of Three Hundred Fifteen Thousand (\$315,000) Dollars, which Note evidences Lime Ridge's obligation to pay to Industries the deferred portion of the purchase price for the aforementioned shares.

Exhibit C

XXIX-001S

Ex. 9
82 of 126

B. Industries is unwilling to sell the aforementioned shares of capital stock of Safety Light to Lime Ridge unless Safety Light guarantees payment and performance of Lime Ridge's obligations under the Note.

NOW, THEREFORE, in consideration of the Recitals and the mutual covenants herein contained, and in order to induce Industries to consummate the transactions contemplated by the Stock Purchase Agreement, the parties hereto agree as follows:

1. Definition

The term "Obligations to Industries" shall mean (i) the indebtedness of Lime Ridge to Industries as evidenced by the Note, and any and all extensions, modifications, substitutions, renewals, increases and changes in the form thereof; and (ii) all costs and expenses (including attorneys' fees) incurred and/or paid by Industries in enforcing its rights pursuant to the Note.

2. Guaranty of Obligations to Industries

2.1 The Guarantor hereby unconditionally guaranties to Industries the due and punctual payment and performance by Lime Ridge of all of the Obligations to Industries, whether as a result of acceleration, maturity or otherwise. The Guarantor agrees that if Lime Ridge shall fail to pay any Obligation to

Industries when and as the same shall become due and payable, the Guarantor will cause such amount to be paid when and as the same shall become due and payable.

2.2 The Guarantor shall be primarily liable with Lime Ridge for the payment and performance of the Obligations to Industries. It is expressly agreed to and understood by the Guarantor that Industries, upon the occurrence of a default or an Event of Default under the Note, need not look first to Lime Ridge for payment of the obligations guaranteed hereby, and that Industries need not exhaust or proceed against Lime Ridge's assets before proceeding against the Guarantor.

2.3 The obligations of the Guarantor hereunder are absolute and unconditional, irrespective of any circumstances which might constitute a legal or equitable defense or discharge of a guarantor or surety, or which might otherwise limit enforceability against the Guarantor by Industries.

2.4 The obligations of the Guarantor hereunder and the right of Industries to enforce the same shall not in any way be affected by the discharge of Lime Ridge or the Guarantor from the obligations guaranteed hereby pursuant to any insolvency, bankruptcy, liquidation, reorganization, readjustment,

composition or other proceeding involving or affecting Lime Ridge or the Guarantor.

2.5 Industries may deal with Lime Ridge and the Guarantor in the same manner and as freely as if this Guaranty did not exist, and shall be entitled, inter alia, to grant to Lime Ridge such extension or extensions of time to perform any act or acts as it may deem advisable, at any time, and from time to time, without terminating, affecting or impairing the validity of this Section 2 or the obligations of the Guarantor hereunder.

2.6 No compromise, alteration, amendment, modification, extension, renewal, release or other change or waiver, consent or any other action, or delay, or omission or failure to act, in respect of any liability or obligation guaranteed by the Guarantor hereunder, shall in any way affect or alter the obligations of the Guarantor hereunder.

2.7 The Guarantor hereby expressly and irrevocably waives all claims of waiver, release, surrender, alteration or compromise and all defenses, set-offs, counterclaims, recoupments, reductions, limitations, impairments or terminations, whether arising under this Section 2 or otherwise.

2.8 The Guarantor waives any right, or claim of right, to cause a marshalling of its assets or of Lime Ridge's assets or to proceed against them in any particular order, it being understood that Industries shall be under no obligation whatsoever to proceed first against Lime Ridge's assets before proceeding against the Guarantor, or to proceed first against the Guarantor before proceeding against Lime Ridge's assets.

3. Responsibility for Expenses

The Guarantor shall be liable for all costs and expenses, including attorneys' fees and disbursements, incurred by Industries in enforcing the Guarantor's obligations hereunder.

4. Miscellaneous

4.1 This Guaranty represents the entire understanding of the parties hereto with respect to the subject matter hereof, and may not be amended or modified in any manner, at any time, unless by a writing executed by all of the parties hereto.

4.2 This Guaranty shall be binding upon and shall inure to the benefit of the parties hereto, and their respective heirs, successors, legal representatives, and assigns.

4.3 This Guaranty shall be construed in accordance with and shall be governed by the laws of the Commonwealth of Pennsylvania.

4.4 All paragraph headings in this Guaranty are for convenience of reference only and shall not be deemed a part of this Guaranty.

4.5 All notices to be given hereunder shall be given by certified mail, return receipt requested, addressed to the parties hereto at their addresses set forth above, or at such other address as they shall designate in writing, and shall be deemed given when mailed.

IN WITNESS WHEREOF, Safety Light Corporation has executed this Guaranty by its duly authorized corporate officers the day and year first above written.

ATTEST:

SAFETY LIGHT CORPORATION


DAVID JOHN WATTS, Vice President

By  (L.S.)
JOHN T. MILLER, President

Grant
Miller

Pres.
Safety Dept.

SECURITY AGREEMENT

This Security Agreement is made this 24th day of May, 1982, between USR INDUSTRIES, INC., a Delaware corporation, having offices at Suite 217, 2203 Timberloch Place, The Woodlands, Texas 77380 ("Secured Party"), SAFETY LIGHT CORPORATION, a Delaware corporation, having offices at 4150 A Old Berwick Road, Bloomsburg, Pennsylvania ("Safety Light"), and LIME RIDGE INDUSTRIES, INC., a Pennsylvania corporation having offices at 4150 A Old Berwick Road, Bloomsburg, Pennsylvania ("Lime Ridge").

RECITALS:

A. Concurrently with the execution hereof, the following has transpired:

(i) Secured Party has sold to Lime Ridge, pursuant to the terms of a Stock Purchase Agreement, of this date, all of the issued and outstanding shares of capital stock ("Shares") of Safety Light Corporation, a Delaware corporation.

(ii) Lime Ridge has executed and delivered to Secured Party its promissory note ("Note"), in the principal sum

Exhibit D

XXIX-001 T

Ex. 9
88 of 126

of Three Hundred Fifteen Thousand (\$315,000) Dollars, which Note evidences its obligation to pay the deferred portion of the purchase price for the Shares;

(iii) Safety Light has executed and delivered to Secured Party a Guaranty of Payment ("Guaranty"), pursuant to which it has guaranteed payment of the obligations of Lime Ridge under the Note.

B. Secured Party is unwilling to sell the Shares to Lime Ridge unless Safety Light secures its obligations to guaranty by granting to Secured Party a security interest in the collateral more fully described herein, and unless Lime Ridge secures its obligations under the Note by granting to Secured Party a security interest in the collateral more fully described herein.

C. As provided for in the Stock Purchase Agreement, Lime Ridge has covenanted that it will, within 90 days from the date hereof, merge Lime Ridge into Safety Light, with Safety Light being the surviving corporation.

NOW, THEREFORE, in consideration of the Recitals, and

the mutual covenants herein contained, the parties hereto agree as follows:

1. Granting of Security Interests

1.1 (a) As collateral security for (i) the obligations of Safety Light to guarantee to Secured Party the "Obligations to Industries" (as that term is defined in the Guaranty) and (ii) all costs and expenses incurred and/or paid by the Secured Party in enforcing its rights pursuant to the Guaranty and this Agreement, Safety Light hereby grants, pledges, transfers, assigns and sets over unto Secured Party a security interest in the Collateral (as hereinafter defined).

(b) As collateral security for (i) the due and punctual payment of the Note and any and all increases, extensions, renewals, substitutions and changes in the form thereof; (ii) the full, prompt and unconditional performance of all obligations, covenants, warranties, representations, promises and liabilities of Lime Ridge pursuant to the Stock Purchase Agreement, the Note, this Agreement, and any other agreement executed and/or delivered by Lime Ridge in connection with the transactions contemplated by the Stock Purchase Agreement; and (iii) all

costs and expenses incurred and/or paid by Secured Party in enforcing its rights pursuant to the Note, Stock Purchase Agreement, and this Agreement, Lime Ridge hereby grants, pledges, transfers, assigns and sets over unto Secured Party a security interest in the Collateral (as hereinafter defined).

(c) The obligations secured hereby are sometimes hereinafter collectively referred to as the "Obligations".

1.2. The term "Collateral" shall mean all of Lime Ridge's and/or Safety Light's right, title and interest in the Equipment (as hereinafter defined), the Inventory (as hereinafter defined), and the Accounts Receivable (as hereinafter defined), together with all proceeds and products of the same.

1.3. (a) The term "Equipment" shall mean, in addition to the definition thereof contained in the Uniform Commercial Code of the Commonwealth of Pennsylvania, all equipment, machinery, fixtures, and all other tangible assets, all replacements, repairs, modifications, alterations, additions, controls and operating accessories therefor, all substitutions and replacements therefor, and all accessions and additions thereto and products and proceeds of the foregoing, whether now owned or

hereafter acquired by Safety Light and/or Lime Ridge.

(b) The term "Inventory" shall mean, in addition to the definition thereof contained in the Uniform Commercial Code of the Commonwealth of Pennsylvania, all goods, merchandise, or other personal property held by Lime Ridge and/or Safety Light for sale or lease or to be furnished under contracts of service or which have been so furnished, all labels and other devices, names, or marks affixed thereto for purposes of selling or identifying the same or the seller or manufacturer thereof, all right, title and interest of Lime Ridge and/or Safety Light therein, all raw materials, work or goods in process or materials and supplies of every nature used, consumed or to be consumed in Lime Ridge's and/or Safety Light's business, all packaging and shipping materials and proceeds and products of any of the foregoing, whether now owned or hereafter acquired by Lime Ridge and/or Safety Light.

(c) The term "Accounts Receivable" shall mean in addition to the definition thereof contained in the Uniform Commercial Code of the Commonwealth of Pennsylvania, any and all obligations of any kind at any time due and/or owing to Lime Ridge and/or Safety Light and all rights of either of them to

receive payment or any other consideration (whether classified under the Uniform Commercial Code of the Commonwealth of Pennsylvania or any other state, as accounts, contract rights, chattel paper, general intangibles, or otherwise) including, without limitation, invoices, contract rights, accounts receivable, general intangibles, choses in action, notes, drafts, acceptances, instruments and all other debts, obligations and liabilities in whatever form owing to Lime Ridge and/or Safety Light from any person, firm, governmental authority, corporation, or any other entity, or security therefor, and all of their rights to goods sold (whether delivered, undelivered, in transit or returned), which may be represented thereby, whether now existing or hereafter arising, together with all proceeds and products of any and all of the foregoing.

2. Affirmative Covenants

Until payment in full of all Obligations, Lime Ridge and Safety Light covenant and agree that they will:

2.1. Promptly pay when due all indebtedness, sums and liabilities of any kind now or hereafter owing by either of them to any party however created, incurred, evidenced, acquired,

arising or payable, including without limitation the Obligations, income and excise taxes and taxes with respect to any of the Collateral, or any wages or salaries paid by either of them or otherwise.

2.2. Observe, perform and comply with the covenants, terms and conditions of this Agreement, the Stock Purchase Agreement, Note, and any other agreement or document entered into between either of them and the Secured Party in connection with the transactions contemplated by the Stock Purchase Agreement.

2.3. Maintain and preserve, and cause any subsidiary to maintain and preserve, in full force and effect, their corporate existence and rights, franchises, licenses, and qualifications necessary to continue its business, and comply with all applicable statutes, rules and regulations pertaining to the operation, conduct and maintenance of its existence and business.

2.4. Furnish to Secured Party:

(a) As soon as delivered to any other creditor of Safety Light and/or Lime Ridge, but in no event later than forty-five (45) days after the end of each of their quarterly fiscal

periods except the fourth, their respective balance sheets as at the end of such period, and their respective cumulative income and surplus statement for the period beginning on the first day of such fiscal year and ended on the date of such balance sheet, all in reasonable detail, all prepared in accordance with generally accepted accounting principles consistently applied, and all certified by their chief financial officers.

(b) As soon as delivered to any other creditor of Safety Light and/or Lime Ridge, but in no event later than ninety (90) days after the end of each of their respective fiscal years, their respective balance sheets as at the end of such year, and their income and surplus statements for such fiscal year, all in reasonable detail, all prepared in accordance with generally accepted accounting principles consistently applied, and all certified by their respective officers and directors which certification shall be in form substantially similar to that executed and delivered by Secured Party to its independent certified public accountants in connection with such accountants auditing of the books and records of Secured Party.

2.5. At any time and from time to time, upon request of Secured Party, give representatives of Secured Party access dur-

ing normal business hours to, and permit any of them to examine, audit, copy or make extracts from, any and all books, records, and documents in the possession of Safety Light and/or Lime Ridge relating to their respective affairs, and to inspect any of their property wherever located.

2.6. Comply with all applicable laws, rules, regulations and orders of any governmental authority, compliance with which is necessary to maintain their respective corporate existence, the conduct of their business or non-compliance with which would materially adversely affect their ability to perform the Obligations or any security given to Secured Party to secure the Obligations.

2.7. (a) Cause to be maintained, in full force and effect on all property given as collateral security for all Obligations, insurance against such risks as is satisfactory to Secured Party, including, without limitation, fire, theft, burglary, pilferage, loss in transit and hazard insurance. Said insurance policy or policies shall:

(i) be in amounts not less than the greater of (A) \$200,000 or (B) such amount

which will preclude Safety Light and/or Lime Ridge from being a co-insurer within the terms of the applicable policies;

(ii) be in a form and with insurers which are reasonably satisfactory to Secured Party;

(iii) designate Secured Party and its assignees as additional loss payees as their interests shall from time to time appear;

(iv) contain a "breach of warranty" clause whereby the insurer agrees that a breach of the insuring conditions or any negligence by Safety Light and/or Lime Ridge or any other person shall not invalidate the insurance as to the Secured Party and its assigns;

(v) provide that they may not be cancelled or materially altered without thirty

(30) days' written notice to Secured Party and its assigns; and

(vi) upon demand, be delivered to Secured Party.

(b) Obtain such additional insurance as Secured Party may require.

(c) In the event of loss or damage forthwith notify Secured Party and file proofs of loss with the appropriate insurers. Lime Ridge and Safety Light hereby authorize Secured Party to endorse any checks or drafts constituting insurance proceeds.

2.8. Maintain all property in which Secured Party has been granted a security interest hereunder as collateral security for any Obligations in good condition and repair at all times, preserve it against any loss, damage or destruction of any nature whatsoever relating to said property or its use, and keep said property free and clear of any liens and encumbrances whatsoever, except those liens and encumbrances created or permitted pursuant hereto.

2.9. At any time and from time to time upon request of Secured Party, execute and deliver such further documents and do such other acts and things as Secured Party may reasonably request in order to effectuate more fully the purposes of this Agreement.

2.10. In the event of the occurrence of an Event of Default, pay any and all legal fees, expenses and disbursements reasonably and necessarily incurred by or on behalf of the Secured Party in connection with the transactions contemplated by this Agreement.

2.11. At all time keep accurate and complete records of the Collateral.

3. Negative Covenants

Until payment in full of all Obligations, Safety Light and Lime Ridge covenant and agree that they will not:

3.1. Consolidate with, merge with, or acquire the stock or assets of any person, firm, joint venture, partnership, cor-

poration or any other entity, whether by merger, consolidation, purchase of stock or otherwise except for the merger of Safety Light with Lime Ridge.

3.2. Sell, lease or otherwise dispose of any or all of their assets or property, other than (i) the sale or lease of the Inventory in the ordinary course of business or (ii) the sale or disposition of Equipment, provided that such Equipment is replaced with Equipment of like value (there being subtracted from said value, the amount of any purchase money security interest granted in connection with Lime Ridge's or Safety Light's acquisition of the same).

3.3. Incur, create or permit to exist any mortgage, assignment, pledge, hypothecation, security interest, lien or other encumbrance on any of their property or assets, whether now owned or hereafter acquired, except for (i) those liens in favor of Secured Party created by this Agreement and (ii) purchase money security interests granted in connection the purchase of Equipment.

3.4. Incur, create, assume or permit to exist any indebtedness or liability on account of either borrowed money or

the deferred purchase price of property in excess, at any point in time, of \$50,000.

3.5. Make loans to any person, firm or entity.

3.6. Assume, guarantee, endorse, contingently agree to purchase or otherwise become liable upon the obligations of any firm or entity.

3.7. Remove, or cause, or permit to be removed, without Secured Party's prior written consent, any of their property or assets from those premises set forth on Schedule 1 attached hereto, except for sales of Inventory in the ordinary course of its business and except for the sale or disposition of Equipment if replaced with Equipment of like value.

3.8. Sell, assign, transfer, discount, settle, compromise or otherwise dispose of any Accounts Receivable or any promissory note payable to either of them with or without recourse, except for collection without recourse in the ordinary course of business.

3.9. Declare or pay any cash dividend or make cash

distributions on or redeem, retire or otherwise acquire directly or indirectly, any share of their stock without the prior written consent of Secured Party.

3.10. Materially change or alter the nature of their respective business.

3.12. Change the location of their principal place of business and/or place where their books and records are maintained, without the prior written consent of the Secured Party.

3.13. Cause, suffer, or permit Net Working Capital (as hereinafter defined) to be or become less than _____ (\$ _____) Dollars. The term "Net Working Capital" shall mean as of the time of any determination thereof, the amount, determined in accordance with generally accepted accounting principles, applied on a consistent basis, by which the current assets of Safety Light (and after the merger of Safety Light and Lime Ridge, of the survivor thereof) exceed its current liabilities.

3.14. Cause, suffer or permit Tangible Net Worth (as hereinafter defined) to be or become less than _____

_____ (\$ _____) Dollars. The term "Tangible Net Worth" shall mean as of the time of any determination thereof, the difference between (A) the sum of (i) the par value (or value stated on the books of the Debtor) of the capital stock of all classes of Debtor, plus (or minus in case of a deficit) (ii) the amount of the surplus, whether capital or earned, of Debtor and its subsidiaries, less (B) the sum of treasury stock, unamortized debt discount and expense, goodwill, trademarks, trade names, patents, deferred charges and other intangible assets and any write-up of the value of any assets, all as determined in accordance with generally accepted accounting principles, applied on a consistent basis. The term "Debtor" as used herein shall mean, prior to the merger of Safety Light with Lime Ridge, Safety Light, and subsequent to the aforesaid merger, the survivor of such merger.

4. Events of Default

The occurrence of any of the following shall constitute an Event of Default hereunder:

4.1. If Lime Ridge and/or Safety Light fails to make, when due, any payment required by this Agreement, the Note, the

Stock Purchase Agreement or any other document and/or instrument executed and/or delivered by either of them in connection with the transactions contemplated by the Stock Purchase Agreement.

4.2. If Lime Ridge and/or Safety Light fails to observe or perform any covenant, term or condition of this Agreement, the Note, the Stock Purchase Agreement, or any other document and/or instrument executed and/or delivered by either of them in connection with the transactions contemplated by the Stock Purchase Agreement.

4.3. The occurrence of any default on any of the Obligations, or any default on any other loans made to Lime Ridge or Safety Light by third parties.

4.4. If Lime Ridge and/or Safety Light ceases to do business as a going concern, or there is filed by or against either of them any petition with respect to their own financial condition under any bankruptcy law or any amendment thereto including, without limitation a petition for reorganization, arrangement or extension, or under any other insolvency laws providing for the relief of debtors.

4.5. A receiver, trustee, conservator or liquidator is appointed for Lime Ridge and/or Safety Light, or all or a substantial part of their assets; or either of them shall be adjudicated bankrupt, insolvent or in need of any relief provided for debtors by any court.

4.6. If any judgment or judgments (except those covered by insurance), or any levy, sequestration, or attachment, which in the aggregate exceeds \$10,000, against Lime Ridge and/or Safety Light or their property, remains unpaid, undischarged, unsatisfied, unbonded or undismissed for a period of thirty (30) days after they have received notification of the entry thereof.

4.7. If there occurs any change in the condition or affairs, financial or otherwise, of Safety Light and/or Lime Ridge or of any endorser, guarantor or surety for the liability of either of them to Secured Party which in the opinion of Secured Party impairs Secured Party's security or increases its risk.

4.8. If at any time less than 100% of the issued and outstanding voting stock of Lime Ridge shall not be owned by John T. Miller, Charles R. White and/or David John Watts, or an entity

in which such persons own 100% of the issued and outstanding stock.

4.9. The liquidation and/or dissolution of Lime Ridge or Safety Light, except pursuant to the merger of Safety Light with Lime Ridge.

4.10. The occurrence of a default or Event of Default under the Note.

5. Remedies

5.1. (a) Upon the occurrence of an Event of Default the total amount (the "Default Amount") of (i) the aggregate amount of all Obligations for principal and interest, including late charges thereon, and other sums which are then due and unpaid; and (ii) an amount equal to the aggregate amount of all principal remaining to be repaid on all Obligations; (iii) interest on the foregoing sums at the rate of Eighteen (18%) per cent per annum from said occurrence until paid in full shall, at the option of Secured Party, become immediately due and payable without notice or demand; and

(b) Secured Party may forthwith give written notice to Safety Light and/or Lime Ridge, whereupon they shall, at their expense, promptly deliver any and all Collateral to such place as Secured Party may designate, or Secured Party shall have the right to enter upon the premises where the Collateral is located and take immediate possession of and remove the Collateral without liability to Safety Light and/or Lime Ridge except such as is occasioned by the gross negligence of Secured Party, its employees or agents. In the event Secured Party obtains possession of the Collateral, Secured Party may sell any or all of the Collateral at public or private sale, at such price or prices as Secured Party may deem best, either for cash, on credit, or for future delivery, in bulk or in parcels, and/or lease or retain Collateral repossessed using it or keeping it idle. Secured Party may also elect to retain the Collateral or any part thereof in satisfaction of the Obligations. The proceeds, if any, of any such sale or leasing by Secured Party shall be applied: First, to the payment of all fees and expenses incurred by Secured Party as a result of such Events of Default, including, without limitation, any legal fees and expenses incurred in repossessing the Collateral and selling and/or leasing it; Second, to pay the Default Amount to the extent not previously paid by Safety Light and/or Lime Ridge; and Third, to pay any

excess remaining to Safety Light and/or Lime Ridge.

5.2. At all times prior and subsequent to an Event of Default and in addition to the foregoing, the Secured Party shall be entitled to all of the rights and remedies of a secured party under the Uniform Commercial Code as enacted in Pennsylvania, with respect to all Collateral given pursuant to the terms of this Agreement.

5.3. No remedy referred to herein is intended to be exclusive but shall be cumulative and in addition to any other remedy referred to above or otherwise available to Secured Party at law or in equity. No express or implied waiver by Secured Party of any default or Event of Default shall in any way be construed to be, a waiver of any future or subsequent default or Event of Default. The failure or delay of Secured Party in exercising any rights granted hereunder upon any occurrence of any of the contingencies set forth herein shall not constitute a waiver of any such right upon the continuation or recurrence of any such contingencies or similar contingencies and any single or partial exercise of any particular right by Secured Party or any other right provided herein. Secured Party shall be under no obligation to proceed against any or all of the Collateral before in-

stituting proceedings against Lime Ridge under the Note or against Safety Light under the Guaranty.

5.4. Secured Party shall be under no obligation whatsoever to proceed first against any of the Collateral (or any other collateral given by any other party to secure the Obligations) before proceeding against any other Collateral. It is understood and agreed that all Collateral stands as equal security for all Obligations, and that Secured Party shall have the right to proceed against any or all of the Collateral in any order, simultaneously, as it, in its sole discretion, shall determine.

6. Other Charges to be Paid to Secured Party

In addition to the principal and interest of the Obligations, Safety Light and Lime Ridge shall pay to Secured Party, upon demand, together with interest at the rate of Eighteen (18%) per cent per annum from the date when incurred or advanced by Secured Party until repaid by them, all costs, expenses or other sums incurred or advanced by Secured Party to preserve, collect, protect its interest in or realize on the Collateral, and to enforce Secured Party's rights as against Safety Light and/or

Lime Ridge, any account debtor or guarantor, or in the prosecution or defense of any action or proceeding related to the subject matter of this Agreement. All such expenses, costs and other sums shall be deemed secured by the Collateral.

7. Miscellaneous Rights of Secured Party

7.1. At any time after an Event of Default hereunder Secured Party may notify the account debtors on any of the Accounts Receivable to make payments directly to Secured Party, and Secured Party may endorse all items of payment received by it which are payable to Safety Light and/or Lime Ridge. Safety Light and Lime Ridge, at the request of Secured Party, shall notify the account debtors of Secured Party's security interest in their Accounts Receivable.

7.2. At all times prior and subsequent to an Event of Default hereunder, Secured Party shall be entitled to all the rights and remedies of a Secured Party under the Uniform Commercial Code as enacted in Pennsylvania, with respect to all Collateral.

7.3. At all times subsequent to an Event of Default

hereunder, Secured Party may take any and all action which in its sole discretion is necessary and proper to preserve its interest in the Collateral, including, without limitation, the payment of debts which might, in Secured Party's sole discretion, impair the Collateral or Secured Party's security interest therein, purchasing insurance on the Collateral, repairing the Collateral, or paying taxes or assessments thereon, and the sums so expended by Secured Party shall be deemed secured by the Collateral, shall be added to the amount of the Obligations due Secured Party, and shall be payable on demand with interest at the rate of Eighteen (18%) per cent per annum from the date expended by Secured Party and until repaid.

7.4. From and after an Event of Default, Secured Party is authorized to notify the postal authorities to deliver all mail, correspondence or parcels addressed to Safety Light and/or Lime Ridge to Secured Party at such address as Secured Party may direct.

8. Further Assurances

8.1. Safety Light and Lime Ridge shall take such steps and execute and deliver such financing statements and other docu-

ments all in form and substance satisfactory to Secured Party relating to the creation, validity, or perfection of the security interest provided for herein, under the Uniform Commercial Code or any other laws of the Commonwealth of Pennsylvania or of any other state or states as Secured Party may from time to time require.

8.2. Secured Party is hereby irrevocably appointed by Safety Light and Lime Ridge as their lawful attorney and agent in fact to execute financing statements and other documents and agreements as Secured Party may deem necessary for the purpose of perfecting any security interest, mortgages or liens under any applicable law. Further, Secured Party is hereby authorized to file on behalf of Safety Light and/or Lime Ridge, in their name, and at their expense, such financing statements, documents or agreements in any appropriate governmental office. Secured Party shall give Safety Light and/or Lime Ridge notice of any filings made hereunder. In addition, Safety Light and Lime Ridge hereby grant a power of attorney to Secured Party to endorse their names on checks, notes, acceptances, drafts, and any other instruments requiring their endorsement, to change the address where their mail should be sent and to open all mail. The powers of attorney granted to Secured Party in this Agreement are coupled with an

interest and are irrevocable so long as this Agreement is in force.

9. Miscellaneous

9.1. This Agreement shall be binding upon and shall inure to the benefit of the parties hereto and their respective successors, assigns, heirs, administrators and executors.

9.2. This Agreement shall be governed by and shall be construed in accordance with the laws of the Commonwealth of Pennsylvania.

9.3. Section headings contained in this Agreement are for convenience of reference only and shall not be deemed a part of this Agreement.

9.4. This Agreement may not be modified, changed, amended or terminated except in writing, signed by the parties hereto.

9.5. Any notification of a sale or other disposition of Collateral, or any other acts by Secured Party required to be given by Secured Party, shall be sufficiently given if given not

less than three (3) days prior to the dates on which such sales or other disposition would be made, and such notification shall be deemed commercially reasonable notice.

IN WITNESS WHEREOF the parties hereto have, by their duly authorized corporate officers, executed this Agreement the day and year first above written.

ATTEST:

USR INDUSTRIES, INC.

By *J. H. Wilson*

By *Robert T. McGovern*

ATTEST:

SAFETY LIGHT CORPORATION

By *David John Watts*
DAVID JOHN WATTS, Vice President

By *John T. Miller*
JOHN T. MILLER, President

ATTEST:

LIME RIDGE INDUSTRIES, INC.

By *David John Watts*
DAVID JOHN WATTS, Vice President

By *John T. Miller*
JOHN T. MILLER, President

John T.
Mullen

Pres. of
Safety Light &
Lamp Co.

SECRETARY'S CERTIFICATE

The undersigned, being the duly elected Secretary of USR Industries, Inc., a corporation formed pursuant to the laws of the State of Delaware, does hereby certify that the following resolutions were adopted by the Board of Directors of said corporation by unanimous consent in lieu of the holding of a special meeting of the Corporation's Board Of Directors, which resolutions remain in full force and effect as of the date hereof without modification or amendment in any respect:

RESOLVED, that the Corporation sell to Lime Ridge Industries, Inc., a Pennsylvania corporation, pursuant to and in accordance with the terms of a Stock Purchase Agreement, in substantially the same form as that submitted to and reviewed by all of the Corporation's directors, all of the issued and outstanding shares of capital stock of Safety Light Corporation, a Delaware corporation owned by the Corporation.

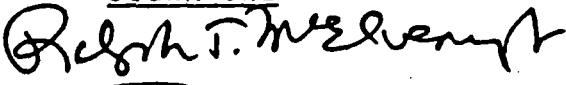
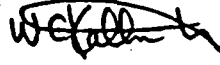
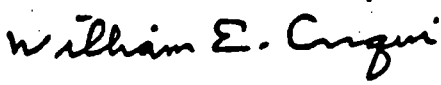
RESOLVED, that the Assistant Treasurer, Secretary, and President of this Corporation be and they hereby are authorized and directed on behalf of the Corporation to take all steps necessary and appropriate to consummate and effect the aforesaid stock sale pursuant to the terms of the Stock Purchase Agreement and in that regard, to execute all documents appropriate thereto.

XXIX-001 u

Ex. 9
115 of 126

The undersigned hereby further certifies as follows:

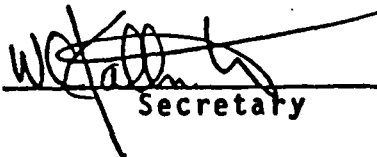
1. That the following are true and correct specimens of the signatures of:

<u>NAME</u>	<u>TITLE</u>	<u>SIGNATURE</u>
Ralph T. McElvenny, Jr.	President	
William C. Kaltnecker	Secretary	
William E. Criqui	Assistant Treasurer	

2. The above-mentioned officers are, as of the date hereof, duly elected and qualified and acting as officers of the Corporation, holding the offices set opposite their names above.

3. The above-mentioned officers are duly authorized to execute and deliver any and all documents necessary for or relating to the aforesaid transactions and to take any and all actions on behalf of this Corporation in connection with the transactions and documents contemplated by the foregoing.

IN WITNESS WHEREOF, the undersigned has executed this Certificate and affixed the seal of the Corporation as of the 24 day of May, 1982


Secretary

UNANIMOUS CONSENT OF DIRECTORS

OF

USR INDUSTRIES, INC.

* * * * *

The undersigned, being all of the directors of USR Industries, Inc., a Delaware corporation, hereby take the following action by unanimous consent in lieu of holding a special meeting of the Corporation's Board of Directors:

RESOLVED, that the Corporation sell to Lime Ridge Industries, Inc., a Pennsylvania corporation, pursuant to and in accordance with the terms of a Stock Purchase Agreement, in substantially the same form as that reviewed by all of the Corporation's directors, all of the issued and outstanding shares of capital stock of Safety Light Corporation, a Delaware corporation, owned by the Corporation.

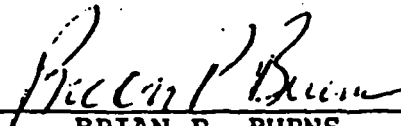
RESOLVED, that the Assistant Secretary, Secretary and President of this Corporation be and they hereby are authorized and directed on behalf of the Corporation to take all steps necessary and appropriate to consummate and effect the aforesaid stock sale pursuant to the terms of the Stock Purchase Agreement and in that regard, to execute all documents appropriate thereto.

The undersigned, by affixing their signatures hereto

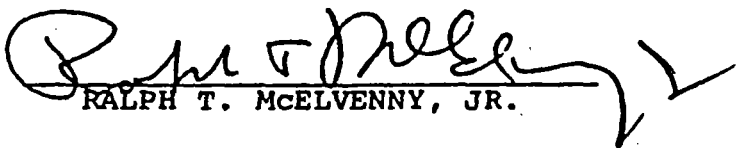
XXIX-001 ✓

Ex. 9
117 of 126

this 24th day of May, 1982, do hereby consent to,
authorize and approve the foregoing resolutions in their
capacity of all of the directors of USR Industries, Inc.


BRIAN P. BURNS

JOSEPH KOSTRZEWA


RALPH T. McELVENNY, JR.

DATED:

May 24, 1982

UNANIMOUS CONSENT OF DIRECTORS

OF

USR INDUSTRIES, INC.

* * * * *

The undersigned, being all of the directors of
USR Industries, Inc., a Delaware corporation, hereby take
the following action by unanimous consent in lieu of hold-
ing a special meeting of the Corporation's Board of Directors:

RESOLVED, that the Corporation
sell to Lime Ridge Industries, Inc., a
Pennsylvania corporation, pursuant to and
in accordance with the terms of a Stock
Purchase Agreement, in substantially the
same form as that reviewed by all of the
Corporation's directors, all of the issued
and outstanding shares of capital stock of
Safety Light Corporation, a Delaware cor-
poration, owned by the Corporation.

RESOLVED, that the Assistant
Treasurer, Secretary and President of this
Corporation be and they hereby are autho-
rized and directed on behalf of the Corpora-
tion to take all steps necessary and appro-
priate to consummate and effect the afore-
said stock sale pursuant to the terms of
the Stock Purchase Agreement and in that
regard, to execute all documents appro-
priate thereto.

The undersigned, by affixing their signatures hereto

XXIX-001W

Ex. 9
119 of 126

this 24th day of May, 1982, do hereby consent to,
authorize and approve the foregoing resolutions in their
capacity of all of the directors of USR Industries, Inc.

BRIAN P. BURNS

Joseph Kostreza
JOSEPH KOSTRZEWA

Ralph T. McElvenny, Jr.
RALPH T. MCELVENNY, JR.

DATED:

May 24, 1982

UNANIMOUS CONSENT OF DIRECTORS

OF

USR INDUSTRIES, INC.

* * * * *

The undersigned, being all of the directors of
USR Industries, Inc., a Delaware corporation, hereby take
the following action by unanimous consent in lieu of hold-
ing a special meeting of the Corporation's Board of Directors:

RESOLVED, that the Corporation
sell to Lime Ridge Industries, Inc., a
Pennsylvania corporation, pursuant to and
in accordance with, the terms of a Stock
Purchase Agreement, in substantially the
same form as that reviewed by all of the
Corporation's directors, all of the issued
and outstanding shares of capital stock of
Safety Light Corporation, a Delaware cor-
poration, owned by the Corporation.

RESOLVED, that the Assistant
Treasurer, Secretary and President of this
Corporation be and they hereby are autho-
rized and directed on behalf of the Corpora-
tion to take all steps necessary and appro-
priate to consummate and effect the afore-
said stock sale pursuant to the terms of
the Stock Purchase Agreement and in that
regard, to execute all documents appro-
priate thereto.

The undersigned, by affixing their signatures hereto

XXIX-001X

Ex. 9
121 of 126

this 24th day of May, 1982, do hereby consent to,
authorize and approve the foregoing resolutions in their
capacity of all of the directors of USR Industries, Inc.

BRIAN P. BURNS

JOSEPH KOSTRZEWA


RALPH T. McELVENNY, JR.

DATED:

May 24, 1982

Uniform Commercial Code - FINANCING STATEMENT - Form UCC-1

IMPORTANT - Read instructions on back before filling out form

This FINANCING STATEMENT is presented to a Filing Officer for filing pursuant to the Uniform Commercial Code.

Page 1 of 4 No. of Additional Sheets Presented: 3

Maturity Date 3. (optional):

1. Debtor(s) (Last Name First and Address(es)):

SAFETY LIGHT CORPORATION
LIME RIDGE INDUSTRIES, INC.
4150 & 4150-A Old Berwick
Road, Bloomsburg, PA 17815
respectively

2. Secured Party(ies): Name(s) and Address(es):

USR INDUSTRIES, INC.

~~Box 248~~

~~Morrisstown, NJ~~

Suite 217, 2203 Timberlake Place
The Woodlands, Texas 77380

4. For Filing Officer: Date, Time No.-Filing Office

5. This Financing Statement covers the following types (or items) of property:

All of the Debtors' right, title and interest in the equipment (as hereinafter defined), the Inventory (as hereinafter defined) and in the Accounts Receivable (as hereinafter defined).

6. Assignee(s) of Secured Party and Address(es)

See additional sheets attached hereto & made part hereof

☒ Proceeds-

☐ Products of the Collateral are also covered.

☐ The described crops are growing or to be grown on:
 ☐ The described goods are or are to be affixed to:
 ☐ (Describe Real Estate Below).

8. Describe Real Estate Here:

9. Name(s) of Record Owner(s):

No. & Street

Town or City

County

Section

Block

Lot

10. This statement is filed without the debtor's signature to perfect a security interest in collateral (check appropriate box)

☐ already subject to a security interest in another jurisdiction when it was brought into this state, or

☐ which is proceeds of the original collateral described above in which a security interest was perfected:

SAFETY LIGHT CORPORATION

By *John T. Miller*
LIME RIDGE INDUSTRIES, INC.

USR INDUSTRIES, INC.

Signature(s) of Debtor(s)

Signature(s) of Secured Party(ies)

(1) FILING OFFICER COPY - NUMERICAL

STANDARD FORM - FORM UCC-1 - Approved by the Secretary of the Commonwealth of Pa.

XXIX-0017

Ex. 9
123 of 126

Uniform Commercial Code—ADDITIONAL SHEET—Form DSCB:UCC-5a (Rev. 11-72) Page 2
Important: Read Instructions

2. Debtor(s) (Last Name First and Address(es)) SAFETY LIGHT CORPORATION LIME RIDGE INDUSTRIES, INC. 4150 & 4150-A Old Berwick Road, Bloomsburg, PA 17815 respectively	3. Secured Party(ies) Name(s) and Address(es) USR INDUSTRIES, INC. Box 246 Morristown, NJ	4. For Filing Office
--	--	----------------------

5. This additional sheet covers the following additional types (or items) of property

1. The "Equipment" shall mean, in addition to the definition thereof contained in the Uniform Commercial Code of the Commonwealth of Pennsylvania, all equipment, machinery, fixtures, and all other tangible assets, all replacements, repairs, modifications, alterations, additions, controls and operating accessories therefor, all substitutions and replacements therefor, and all accessions and additions thereto and products and proceeds of the foregoing, whether now owned or hereafter acquired by the Debtor.

2. The "Inventory" shall mean, in addition to the definition thereof contained in the Uniform Commercial Code of the Commonwealth of Pennsylvania, all goods, merchandise, or other personal property held by the Debtors for sale or lease or to be furnished under contracts of service or which have been so furnished, all labels and other devices, names, or marks affixed thereto for purposes of selling

Ex. 9
124 of 126

Uniform Commercial Code—ADDITIONAL SHEET—Form DSCB:UCC-5a (Rev. 11-72) Page 3 of 4
Important: Read Instructions.

2 Debtor(s) (Last Name First) and Address(es) SAFETY LIGHT CORPORATION LIME RIDGE INDUSTRIES, INC. 4150 & 4150-A Old Berwick Road, Bloomsburg, PA 17815 respectively	3 Secured Party(ies) Name(s) and Address(es) USR INDUSTRIES, INC. Box 246 Morristown, NJ	4 For Filing Officer.
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5. This additional sheet covers the following additional types (or items) of property:

2 continued.....

or identifying the same or the seller or manufacturer thereof, all right, title and interest of the Debtors therein, all raw materials, work or goods in process or materials and supplies of every nature used, consumed or to be consumed in the Debtors' business, all packaging and shipping materials and proceeds and products of any of the foregoing, whether now owned or hereafter acquired by the Debtors.

3. The "Accounts Receivable" shall mean in addition to the definition thereof contained in the Uniform Commercial Code of the Commonwealth of Pennsylvania, any and all obligations of any kind at any time due and/or owing to Debtors and all rights of Debtors to receive payment or any other consideration (whether classified under the Uniform Commercial Code of the Commonwealth of Pennsylvania

Ex. 9
125 of 126

Uniform Commercial Code—ADDITIONAL SHEET—Form DSCB:UCC-5a (Rev. 11-72) 1-000-4-4
Important. Read Instructions.

2 Debtor's (Last Name First and Address(es)) SAFETY LIGHT CORPORATION LIME RIDGE INDUSTRIES, INC. 4150 & 4150-A Old Berwick Road, Bloomsburg, PA 17815 respectively	3 Secured Party(ies) Name(s) and Address(es) USR INDUSTRIES, INC. Box 246 Morristown, NJ	4 For Filing Office
--	---	---------------------

5 This additional sheet covers the following additional types (or items) of property:

3 continued.....

or any other state, as accounts, contract rights, chattel paper, general intangibles, or otherwise) including, without limitation, invoices, contract rights, accounts receivable, general intangibles, choses in action, notes, drafts, acceptances, instruments and all other debts, obligations and liabilities in whatever form owing to Debtor from any person, firm, governmental authority, corporation, or any other entity, or security therefor, and all of its rights to goods sold (whether delivered, undelivered, in transit or returned), which may be represented thereby, whether now existing or hereafter arising, together with all proceeds and products of any and all of the foregoing.

Ex. 9
126 of 126

THIS DOCUMENT IS BEING WITHHELD
FROM PUBLIC DISCLOSURE

DOCUMENT NUMBER: XXIX-002a

License Nos.: 37-00030-02
37-00030-07E
37-00030-08
37-00030-09G
37-00030-10G

3

Safety Light Corp., et al.
ATTN: Jack Miller, President
4150-A Old Berwick Road
Bloomsburg, Pennsylvania 17815
(Identical letter to be sent to each corporation)

Gentlemen:

Subject: Order Modifying License, Effective Immediately, and Demand
for Information

Enclosed is an Order Modifying License, effective immediately, requiring certain activities, including the preparation of a plan, and implementation of that plan, for both site characterization and decontamination of the Bloomsburg facility. In addition, enclosed is a Demand for Information requiring corporate officials from the successor corporations of U.S. Radium Corp. to submit certain information. We recognize that this information may have proprietary value. Therefore, should any corporation submitting information pursuant to this Order desire that such information not be made public, it should follow the procedures set forth in 10 CFR 2.790. In accordance with that regulation, a copy of this letter and the enclosed Order will be placed in the NRC's Public Document Room.

The responses directed by the accompanying Order are not subject to the clearance of the Office of Management and Budget, as required by the Paperwork Reduction Act of 1980, PL 96-511.

Sincerely,

Hugh Thompson, Deputy Executive
Director for Nuclear Materials
Safety, Safeguards and Operations
Support

Enclosure: Order Modifying License and Demand for Information

XXIX-002b

UNITED STATES OF AMERICA
NUCLEAR REGULATORY COMMISSION

In the Matter of:)

Safety Light Corporation)

USR Industries, Inc.)

USR Lighting, Inc.)

USR Chemical, Inc.)

USR Metals, Inc.)

USR Natural Resources, Inc.)

Metreal, Inc.;)

Pinnacle Petroleum, Inc.)

and all other successor)

corporations to either USR)

Industries or U. S. Radium Corp.)

(herein referred to as the)
corporations))

Docket Nos.: 030-05980

030-05982

030-05981

030-08335

030-08444

License Nos.: 37-00030-02

37-00030-08

37-00030-07E

37-00030-09G

37-00030-10G

ORDER MODIFYING LICENSE EFFECTIVE IMMEDIATELY
AND DEMAND FOR INFORMATION

I.

Safety Light Corporation (Safety Light) is the named licensee on Byproduct Material License Nos. 37-00030-02, 37-00030-08 37-00030-07E, 37-00030-09G, and 37-00030-10G, issued by the Nuclear Regulatory Commission (NRC).

License No. 37-00030-02 authorizes the possession, storage, and use of any byproduct material for purposes of decontamination, cleanup, and disposal of equipment and facilities previously used for manufacturing, research and development under this license. License No. 37-00030-02 was originally issued on June 20, 1956 and was last renewed on January 25, 1979. This license has been under timely renewal since February 29, 1984.

XXIX-002c

License No. 37-00030-08 authorizes the licensee to conduct research and development and to manufacture various devices containing tritium. License No. 37-00030-08 was originally issued on August 5, 1969, and was last renewed on January 6, 1983. This license has been under timely renewal since December 31, 1987. The above licenses permit use of material only at facilities at 4150 Old Berwick Road, Bloomsburg, Pennsylvania (the Bloomsburg facility).

License No. 37-00030-07E authorizes the distribution of timepieces, hands and dials to which luminous paint containing tritium is applied, to persons exempt from NRC licensing pursuant to 10 CFR 30.15. License No. 37-00030-07E was originally issued on April 16, 1965 and was last renewed on May 27, 1986. This license expires on April 30, 1991.

License No. 37-00030-09G authorizes the distribution of luminous devices containing tritium to persons generally licensed pursuant to 10 CFR 31.5. License No. 37-00030-09G was originally issued on January 13, 1966 and was last renewed on October 24, 1983. This license has been under timely renewal since October 31, 1988.

License No. 37-00030-10G authorizes the distribution of sealed self-luminous sources to persons generally licensed pursuant to 10 CFR 31.7. License No. 37-00030-10G was originally issued on December 13, 1971 and was last renewed on April 22, 1985. This license expires on April 30, 1990.

II.

On January 21, 1981, the NRC received notification that the NRC licensee known as United States Radium Corporation (U. S. Radium), the prior licensee on all of the above licenses, had changed its name to Safety Light Corporation.

There was no indication at that time that the change involved any ownership or organizational changes. Consequently, routine administrative license amendments changing the corporate name from U. S. Radium Corporation to Safety Light Corporation were issued on March 31, 1982 to modify License No.

37-00030-08; and on January 20, 1983 to modify License Nos. 37-00030-02, 37-00030-07E, 37-00030-09G, and 37-00030-10G.

III.

Since that time, the NRC has obtained and reviewed a May 16, 1980 Agreement and Plan of Merger between U.S. Radium Corporation and USR Industries, Inc. and a July 11, 1980 U.S. Radium letter to its stockholders, ("the 1980 Plan"). Based upon a review of the 1980 Plan, it now appears U.S. Radium, currently doing business as USR Industries, Inc. (Industries), merged with Industries, segregated the activities authorized by the NRC into a separate corporate entity doing business as Safety Light, and then sold that entity to Lime Ridge Industries, Incorporated, a corporation created by former employees of Industries and its predecessor company, U.S. Radium. It specifically appears that the former NRC licensee known as U.S. Radium Corporation, through its officers and directors, created a new corporation, known as USR Industries, Inc. (Industries). The former U.S. Radium merged with Industries, becoming a wholly

owned subsidiary of Industries, and then changed its name to Safety Light Corporation. Industries also transferred all its non-licensed assets and business to five other newly created corporations (USR Lighting, Inc., USR Chemicals, Inc.; USR Metals, Inc.; Metreal, Inc.; and USR Natural Resources, Inc.), then wholly owned subsidiaries to USR Industries. Pinnacle Petroleum, Inc., is apparently another subsidiary of Industries.

IV.

Neither prior notice nor NRC approval were obtained relative to either the 1980 restructuring or subsequent sale, in apparent violation of Section 184 of the Atomic Energy Act and 10 CFR 30.34(b), which prohibit the transfer of a license, either directly or indirectly, unless the NRC shall, after securing full information, give its consent in writing. It further appears from the 1980 Plan that these corporate transactions were an attempt to isolate the liability and responsibility for the cleanup of the Bloomsburg facility from other, assumably more profitable, aspects of U.S. Radium's, and later Industries', business ventures.

Neither U. S. Radium, USR Industries, nor any of their successor corporations or subsidiaries can avoid responsibility and liability for the cleanup of the Bloomsburg facility through the transfer of an NRC license without the consent of the NRC, after full disclosure. Therefore, each of the corporations set forth in Section VI.1. of this Order ("the corporations") are, and remain, jointly and severally liable and responsible for the cleanup of the Bloomsburg

facility and for the conduct of all other activities on that site that require an NRC license.

As early as 1983, the NRC sought clarification from Safety Light relative to corporate transactions that potentially could affect cleanup responsibility. Specifically, the letter that transmitted NRC Inspection Report 83-01, dated September 22, 1983, sought clarification based upon inspections at the Bloomsburg facility, of the effects of an apparent corporate transfer on licensed activity. Safety Lights' November 11, 1983 response to the request in the September 22, 1983 letter appears both incomplete and misleading in that it is silent concerning the details of the 1980 Plan. In its response, Safety Light refers the NRC back to the administrative name change processed in response to their January 21, 1981 submittal and affirmatively states that there were no organizational changes made due to the name change.

On April 20, 1988, the NRC again sought clarification of the relationship of the various corporations with apparent interests in the Bloomsburg facility and the role each would play in the cleanup of that site. In stark contrast to the January 21, 1981 and November 11, 1983 submittals, Industries' June 24, 1988 response concedes that the name change was made concurrently with a corporate reorganization, although even that response fails to state that one purpose of the reorganization was apparently to limit liability, which was stated in the July 11, 1980 U.S. Radium letter to its stockholders.

V.

Prior to the numerous transactions set forth above, on January 25, 1979, the NRC amended License No. 37-00030-02 to include License Condition 14 to require a nine-month plan of specified decontamination activities submitted earlier in a U.S. Radium letter dated October 23, 1978. This letter also stated that a schedule would be developed for decontamination activities beyond the activities specified in the decontamination plan. Condition 13 of License No. 37-00030-02 required U.S. Radium to provide the NRC the status of decontamination efforts and a schedule of work for 12 month periods beginning July 1, 1979. The NRC's inspection at the Bloomsburg facilities on November 12, 1986 and the site contamination survey provided in a letter to the NRC dated February 6, 1987 indicate that the specified decontamination activities were not performed. Furthermore, while Safety Light has provided a report of environmental monitoring each year since 1983, Safety Light has not provided the NRC with the required report of the status of decontamination efforts and schedule of work since License Condition 13 was added to the license.

As a result, by letter dated April 20, 1988, Safety Light, USR Industries, and all other apparent successor corporations to USR Radium were requested to provide a decommissioning plan for the site which would permit the release of the site for unrestricted use. This decommissioning plan was to provide for a final radiological survey that would include all areas where licensed material has been used, stored or buried. The decontamination of the site was permitted to be gradual, extending over a period of ten years, but was to commence within twelve months.

No substantive responses were made to these requests for a plan. By now, the NRC would have expected to have observed action to satisfy the foregoing license conditions. On July 8, 1988, the NRC inspected the Bloomsburg facility and confirmed that there was no current effort underway to decontaminate the facility. Until further information is developed, the NRC considers all corporate successors of U.S. Radium jointly and severally liable for site cleanup, and all other activities requiring a license.

Under the terms of Conditions 13 and 14 of License No. 37-00030-02, as well as the staff's April 20, 1988 letters, the corporations were put on clear notice that decontamination was necessary and required, and were given ample opportunity to submit proposed milestones and plans for decontamination. Rather than formulate and implement a decommissioning plan in response to the 1979 license conditions, it now appears U. S. Radium reorganized in an attempt to limit liability and responsibility for cleanup. Despite repeated efforts by the NRC to get U. S. Radium, and its successors, including, but not limited to Safety Light, to take steps to initiate meaningful decontamination efforts at the Bloomsburg facility, such steps have not been taken.

In order to ensure that the corporations provide adequate resources to evaluate, plan, and implement decontamination efforts with proper radiological safety procedures, I have determined that specific decontamination requirements and milestones are necessary and decontamination needs to begin expeditiously so as to minimize any threat to public health and safety. In view of the corporations' failure to fully meet the terms of Section 184 of the Atomic Energy Act and 10 CFR 30.34(b), as well as other conditions in the license,

though given opportunity to do so, and in view of the need to expeditiously begin decontamination to minimize any threat to public health and safety, I have determined that the NRC lacks reasonable assurance that site characterization and decontamination of the Bloomsburg facility will be initiated and completed in an orderly and timely fashion to assure that the health and safety of the public, including current employees and adjoining landowners, will be protected. This is particularly so in light of the apparent financial inability of any one successor corporation to U. S. Radium to cleanup the Bloomsburg facility. Accordingly, the public health, safety and interest require that the actions required by Section VI of this Order commence immediately. For these reasons and pursuant to 10 CFR 12.201(c), no prior notice is required, and this order should be made immediately effective.

VI.

In view of the foregoing, and pursuant to Sections 81, 161b, 161i, 184 and 186 of the Atomic Energy Act of 1954, as amended, and the Commission's regulations in 10 CFR 2.204 and 10 CFR Part 30, IT IS HEREBY ORDERED, EFFECTIVE IMMEDIATELY, THAT LICENSE NOS. 37-00030-02, 08, 07E, 09G and 10G ARE MODIFIED AS FOLLOWS:

1. The following companies are named on the above licenses and subject to all liabilities under those licenses: Safety Light Corp., USR Industries, Inc., USR Lighting, Inc., USR Chemical, Inc., USR Metals, Inc., USR Natural Resources, Inc., Metreal, Inc., Pinnacle Petroleum, Inc., and all

other successor corporations to, or subsidiaries of, either U.S. Radium Corp. or USR Industries, Inc.

2. Within 90 days from the date of this Order, access shall be controlled to all contaminated areas at the Bloomsburg facility by a fence or other suitable means so as to create a restricted area, as defined in 10 CFR Part 20.
3. Within 30 days from the date of this Order, all corporations set forth in Section VI.1. of this Order shall jointly submit, to the Regional Administrator, NRC, Region I, for his review and approval, a single plan to characterize the radioactivity at the Bloomsburg site. A corporate officer, not lower than the President, from each of the corporations set forth in Section VI.1. of this Order, shall certify under oath or affirmation, to the accuracy of the information contained in the site characterization plan and to the intent on behalf of the corporation to implement the Plan.
4. Within 180 days from the date the Regional Administrator approves the site characterization plan required by Section VI.3. of this Order, all corporations set forth in Section VI.1. of this Order shall jointly submit, to the Regional Administrator, NRC, Region I, for his review and approval, a single report that shall contain a complete radiological characterization of the site, with a description of the location and level of all sources of radiation and contamination. A corporate officer, not lower than the President, for each of the corporations set forth in

Section VI.1. of this Order, shall certify, under oath or affirmation, to the accuracy of the information contained in the site characterization report.

5. Within 30 days from the date the Regional Administrator approves the site characterization report required by Section VI.4. of this Order, all corporations set forth in Section VI.1. of this Order shall jointly submit to the Regional Administrator, NRC, Region I, for his review and approval, a single decontamination plan, with a time table for specific decontamination activities (milestones) and transfer of contaminated waste. A corporate official, not lower than the President, from each of the corporations set forth in Section VI.1. of this Order, shall certify, under oath or affirmation, to the accuracy of the decontamination plan, and to the intent on behalf of the corporation to implement the Plan.
6. Following the Regional Administrator's approval of the Decontamination Plan required by Section VI.5. of this Order, a corporate officer, not lower than the President, from each of the corporations set forth in Section VI.1. of this Order shall submit a monthly status report, under oath or affirmation, to the Regional Administrator of NRC Region I, stating:
 - a. The progress that has been made toward carrying out the decontamination plan during the previous 30 days. In the event that a milestone set forth in the decontamination plan submitted in response to Section VI.5. is not met during the period covered by the report,

the report shall indicate: (1) the date by which the milestone is expected to be accomplished; (2) the reason for the failure to meet the milestone; and (3) the impact that the failure to meet the milestone will have on the decontamination plan and schedule;

- b. The actions under the decontamination plan that are expected to be accomplished within the next 30 days; and,
 - c. The financial resources available during the period covered by the report, including but, not limited to, revenue, costs and expenses, net losses or profits, and sums expended on decontamination of the Bloomsburg facility.
7. No corporation named herein shall either abandon or transfer the Bloomsburg facility or any other corporate asset, of whatever kind or form, until the NRC has confirmed that a successful decontamination of the Bloomsburg facility has been completed.

VI.

Any person adversely affected by this Order may request a hearing within 30 days of the date of its issuance. Any answer to this Order or request for a hearing shall be addressed to the Director, Office of Enforcement, U.S. Nuclear Regulatory Commission, ATTN: Document Control Desk, Washington, DC 20555, with a copy to the Regional Administrator, Region I, 475 Allendale Road, King of Prussia, Pennsylvania 19406. If a hearing is requested by the licensee, the

Commission will issue an Order designating the time and place of hearing. If a hearing is held, the issue to be considered at such hearing shall be whether this Order should be sustained. An answer to this Order or request for hearing shall not stay the effectiveness of this Order. Upon the failure of the licensee or other corporations herein named to answer or request a hearing within the time specified, this order shall be final without further proceedings.

VIII.

Further information is needed to determine whether the Commission can have reasonable assurance that in the future activities at the Bloomsburg facility can be conducted in accordance with the Commission's requirements and the terms of this Order.

Accordingly, to determine whether the licenses should be further modified, suspended or revoked, or other enforcement action taken to ensure compliance with NRC regulatory requirements, within 30 days from the date of this Order, a corporate official, not lower than the President, for each of the corporations shall state in writing, under oath or affirmation, or where appropriate submit, pursuant to Sections 161c and 182 of the Atomic Energy Act of 1954, as amended, and 10 CFR Part 30, answers to the following DEMAND FOR INFORMATION:

1. The names of those individuals (including lawyers) who that official has reason to believe had knowledge of the information set forth in the 1980

Plan and who also was involved in the preparation, or had knowledge of its contents before its issuance, of:

- a. The June 24, 1988 submittals by Safety Light and USR Industries;
 - b. The November 11, 1983 Safety Light submittal in response to Inspection Report 83-01;
 - c. The January 21, 1981 Safety Light submittal advising of the corporate name change.
2. How the decontamination of the Bloomsburg facility was considered, if at all, and by whom, in the course of the several reorganizations and transfers set forth in the documents referenced in Question 1;
3. Copies of all Notices to Stockholders, the Securities and Exchange Commission or other submittals to regulating bodies, stockholders or other persons describing or in any other way related to:
- a. The Agreement to Merge of May 16, 1980;
 - b. The Corporate restructuring of August 1980;
 - c. The Corporate name change in November 1980;
 - d. The sale of Safety Light Corporation in May 1982.

4. Copies of all contracts, agreements, deeds or other instruments of conveyance or agreements between any of the companies or individuals relative to responsibility for cleanup of the Bloomsburg site.
5. Copies of all annual financial statements, including but not limited to, balance sheets showing all assets and liabilities and profit and loss statements, for the three years prior to this Order.
6. Copies of all quarterly financial statements, including but not limited to, balance sheets showing all assets and liabilities and profit and loss statements, for the four quarters prior to this Order.
7. Copies of all annual federal tax returns for the three years prior to this Order.
8. A listing of the names of all individuals or corporations owning at least 10% of the stock in any corporation set forth in Section VII.1. indicating each owner's address and the number of shares owned.

IX.

The Regional Administrator of Region I may modify or relax any provision of the Order or Demand for Information upon the showing of good cause.

FOR THE NUCLEAR REGULATORY COMMISSION

Hugh Thompson, Deputy Executive Director
for Nuclear Materials Safety, Safeguards,
and Operations Support

Dated at Rockville, Maryland
this day of February 1989

4

ACTION PLAN FOR SAFETY LIGHT CORPORATION

<u>ACTION</u>	<u>RESPONSIBILITY LEAD/ASSIST</u>	<u>COMPLETE BY</u>
1. Conduct an inspection at site to determine current status of program, including the licensee's capabilities for the disposal of tritium waste. Include site tour to familiarize Regional Managers with site.	Region I	July 8 (Done)
2. Evaluate USR and Safety Light responses to NRC questions regarding site decontamination responsibility, prepare position about these responses and develop any remaining staff questions.	Region I/OGC	August 5 (Done)
3. Contact Commonwealth of Pennsylvania to inform them of our concerns, findings and plans and to solicit their help and cooperation with respect to radium contamination at the site, as this is not regulated by NRC.	Region I	August 15 (Done) However, see item 8, below
4. Refer issues resulting from evaluation to OI.	Region I	August 19 (Done)
5. Assessment by NMSS to determine the current radiological impact of the contamination at the site and the expected long term impact if the site is abandoned. Use assumptions as necessary. Prepare plan to obtain additional necessary data to improve assessment.	NMSS	September 30 (Done) however, see item 9, below

XXIX-002d

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|-----|---|---------------------|--|
| 6. | Prepare report of OI activities to date and provide copy to Region I. | OI | February 3 |
| 7. | Develop order requiring principal responsible parties to: <ul style="list-style-type: none"> ° Control access to contaminated areas of the site. ° Submit, for NRC approval, a plan to characterize the radioactivity at the site. ° Submit, for NRC approval, a report containing the results of the site characterization study. ° Submit, for NRC approval, a plan, containing milestones, for completing the site decontamination and disposing of the waste. | RI/OGC,
OE, NMSS | Draft to HQ by 1/30/89.
Submit to EDO week of 2/20/89 |
| 8. | Contact Commonwealth of Pennsylvania to inform them of Order. | Region I | Concurrent with notification of licensee |
| 9. | Ensure that the recommendations contained in the NMSS Environmental Evaluation are addressed by Safety Light in its submittals in response to the Order. | Region I | Dependent upon date of submittals by Safety Light |
| 10. | Review Safety Light's Application for Renewal, including effect of continuing tritium discharges on environment. <ul style="list-style-type: none"> ° Develop deficiency questions on routine issues. ° Develop deficiency questions on funding of decommissioning of tritium activities. | Region I | Deferred pending outcome of enforcement action. |

11. Review by NMSS of safety analysis for luminous products produced by Safety Light and development of policy regarding whether the license should require continuing acceptance of returned product for disposal for life of products (even if manufacturing ceases).

NMSS

Deferred.
Involves generic issues and NRC policy issue. Resolution may require rule change.

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DOCUMENT NUMBER: XXIX-003a thru
003e

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DOCUMENT NUMBER: XXIX-004

THIS DOCUMENT IS BEING WITHHELD
FROM PUBLIC DISCLOSURE

DOCUMENT NUMBER: XXIX-005a

UNITED STATES OF AMERICA
NUCLEAR REGULATORY COMMISSION

In the Matter of:)

Safety Light Corporation)

USR Industries, Inc.)

USR Lighting, Inc.)

USR Chemical, Inc.)

USR Metals, Inc.)

USR Natural Resources, Inc.)

Metreal, Inc.;)

Pinnacle Petroleum, Inc.)

and all other successor)

corporations to either USR)

Industries or U. S. Radium Corp.)

(herein referred to as the)

corporations))

Docket Nos.: 030-05980

030-05982

030-05981

030-08335

030-08444

License Nos.: 37-00030-02

37-00030-08

37-00030-07E

37-00030-09G

37-00030-10G

ORDER MODIFYING LICENSE EFFECTIVE IMMEDIATELY
AND DEMAND FOR INFORMATION

I.

Safety Light Corporation (Safety Light) is the named licensee on Byproduct Material License Nos. 37-00030-02, 37-00030-08 37-00030-07E, 37-00030-09G, and 37-00030-10G, issued by the Nuclear Regulatory Commission (NRC).

License No. 37-00030-02 authorizes the possession, storage, and use of any byproduct material for purposes of decontamination, cleanup, and disposal of equipment and facilities previously used for manufacturing, research and development under this license. License No. 37-00030-02 was originally issued on June 20, 1956 and was last renewed on January 25, 1979. This license has been under timely renewal since February 29, 1984.

XXIX - 005b

License No. 37-00030-08 authorizes the licensee to conduct research and development and to manufacture various devices containing tritium. License No. 37-00030-08 was originally issued on August 5, 1969, and was last renewed on January 6, 1983. This license has been under timely renewal since December 31, 1987. The above licenses permit use of material only at facilities at 4150 Old Berwick Road, Bloomsburg, Pennsylvania (the Bloomsburg facility).

License No. 37-00030-07E authorizes the distribution of timepieces, hands and dials to which luminous paint containing tritium is applied, to persons exempt from NRC licensing pursuant to 10 CFR 30.15. License No. 37-00030-07E was originally issued on April 16, 1965 and was last renewed on May 27, 1986. This license expires on April 30, 1991.

License No. 37-00030-09G authorizes the distribution of luminous devices containing tritium to persons generally licensed pursuant to 10 CFR 31.5. License No. 37-00030-09G was originally issued on January 13, 1966 and was last renewed on October 24, 1983. This license has been under timely renewal since October 31, 1988.

License No. 37-00030-10G authorizes the distribution of sealed self-luminous sources to persons generally licensed pursuant to 10 CFR 31.7. License No. 37-00030-10G was originally issued on December 13, 1971 and was last renewed on April 22, 1985. This license expires on April 30, 1990.

II.

On January 21, 1981, the NRC received notification that the NRC licensee known as United States Radium Corporation (U. S. Radium), the prior licensee on all of the above licenses, had changed its name to Safety Light Corporation.

There was no indication at that time that the change involved any ownership or organizational changes. Consequently, routine administrative license amendments changing the corporate name from U. S. Radium Corporation to Safety Light Corporation were issued on March 31, 1982 to modify License No.

37-00030-08; and on January 20, 1983 to modify License Nos. 37-00030-02, 37-00030-07E, 37-00030-09G, and 37-00030-10G.

III.

Since that time, the NRC has obtained and reviewed a May 16, 1980 Agreement and Plan of Merger between U.S. Radium Corporation and USR Industries, Inc. and a July 11, 1980 U.S. Radium letter to its stockholders, ("the 1980 Plan"). Based upon a review of the 1980 Plan, it now appears U.S. Radium, currently doing business as USR Industries, Inc. (Industries), merged with Industries, segregated the activities authorized by the NRC into a separate corporate entity doing business as Safety Light, and then sold that entity to Lime Ridge Industries, Incorporated, a corporation created by former employees of Industries and its predecessor company, U.S. Radium. It specifically appears that the former NRC licensee known as U.S. Radium Corporation, through its officers and directors, created a new corporation, known as USR Industries, Inc. (Industries). The former U.S. Radium merged with Industries, becoming a wholly

owned subsidiary of Industries, and then changed its name to Safety Light Corporation. Industries also transferred all its non-licensed assets and business to five other newly created corporations (USR Lighting, Inc., USR Chemicals, Inc.; USR Metals, Inc.; Metreal, Inc.; and USR Natural Resources, Inc.), then wholly owned subsidiaries to USR Industries. Pinnacle Petroleum, Inc., is apparently another subsidiary of Industries.

IV.

Neither prior notice nor NRC approval were obtained relative to either the 1980 restructuring or subsequent sale, in apparent violation of Section 184 of the Atomic Energy Act and 10 CFR 30.34(b), which prohibit the transfer of a license, either directly or indirectly, unless the NRC shall, after securing full information, give its consent in writing. It further appears from the 1980 Plan that these corporate transactions were an attempt to isolate the liability and responsibility for the cleanup of the Bloomsburg facility from other, assumably more profitable, aspects of U.S. Radium's, and later Industries', business ventures.

Neither U. S. Radium, USR Industries, nor any of their successor corporations or subsidiaries can avoid responsibility and liability for the cleanup of the Bloomsburg facility through the transfer of an NRC license without the consent of the NRC, after full disclosure. Therefore, each of the corporations set forth in Section VI.1. of this Order ("the corporations") are, and remain, jointly and severally liable and responsible for the cleanup of the Bloomsburg

facility and for the conduct of all other activities on that site that require an NRC license.

As early as 1983, the NRC sought clarification from Safety Light relative to corporate transactions that potentially could affect cleanup responsibility. Specifically, the letter that transmitted NRC Inspection Report 83-01, dated September 22, 1983, sought clarification based upon inspections at the Bloomsburg facility, of the effects of an apparent corporate transfer on licensed activity. Safety Lights' November 11, 1983 response to the request in the September 22, 1983 letter appears both incomplete and misleading in that it is silent concerning the details of the 1980 Plan. In its response, Safety Light refers the NRC back to the administrative name change processed in response to their January 21, 1981 submittal and affirmatively states that there were no organizational changes made due to the name change.

On April 20, 1988, the NRC again sought clarification of the relationship of the various corporations with apparent interests in the Bloomsburg facility and the role each would play in the cleanup of that site. In stark contrast to the January 21, 1981 and November 11, 1983 submittals, Industries' June 24, 1988 response concedes that the name change was made concurrently with a corporate reorganization, although even that response fails to state that one purpose of the reorganization was apparently to limit liability, which was stated in the July 11, 1980 U.S. Radium letter to its stockholders.

V.

Prior to the numerous transactions set forth above, on January 25, 1979, the NRC amended License No. 37-00030-02 to include License Condition 14 to require a nine-month plan of specified decontamination activities submitted earlier in a U.S. Radium letter dated October 23, 1978. This letter also stated that a schedule would be developed for decontamination activities beyond the activities specified in the decontamination plan. Condition 13 of License No. 37-00030-02 required U.S. Radium to provide the NRC the status of decontamination efforts and a schedule of work for 12 month periods beginning July 1, 1979. The NRC's inspection at the Bloomsburg facilities on November 12, 1986 and the site contamination survey provided in a letter to the NRC dated February 6, 1987 indicate that the specified decontamination activities were not performed. Furthermore, while Safety Light has provided a report of environmental monitoring each year since 1983, Safety Light has not provided the NRC with the required report of the status of decontamination efforts and schedule of work since License Condition 13 was added to the license.

As a result, by letter dated April 20, 1988, Safety Light, USR Industries, and all other apparent successor corporations to USR Radium were requested to provide a decommissioning plan for the site which would permit the release of the site for unrestricted use. This decommissioning plan was to provide for a final radiological survey that would include all areas where licensed material has been used, stored or buried. The decontamination of the site was permitted to be gradual, extending over a period of ten years, but was to commence within twelve months.

No substantive responses were made to these requests for a plan. By now, the NRC would have expected to have observed action to satisfy the foregoing license conditions. On July 8, 1988, the NRC inspected the Bloomsburg facility and confirmed that there was no current effort underway to decontaminate the facility. Until further information is developed, the NRC considers all corporate successors of U.S. Radium jointly and severally liable for site cleanup, and all other activities requiring a license.

Under the terms of Conditions 13 and 14 of License No. 37-00030-02, as well as the staff's April 20, 1988 letters, the corporations were put on clear notice that decontamination was necessary and required, and were given ample opportunity to submit proposed milestones and plans for decontamination. Rather than formulate and implement a decommissioning plan in response to the 1979 license conditions, it now appears U. S. Radium reorganized in an attempt to limit liability and responsibility for cleanup. Despite repeated efforts by the NRC to get U. S. Radium, and its successors, including, but not limited to Safety Light, to take steps to initiate meaningful decontamination efforts at the Bloomsburg facility, such steps have not been taken.

In order to ensure that the corporations provide adequate resources to evaluate, plan, and implement decontamination efforts with proper radiological safety procedures, I have determined that specific decontamination requirements and milestones are necessary and decontamination needs to begin expeditiously so as to minimize any threat to public health and safety. In view of the corporations' failure to fully meet the terms of Section 184 of the Atomic Energy Act and 10 CFR 30.34(b), as well as other conditions in the license,

though given opportunity to do so, and in view of the need to expeditiously begin decontamination to minimize any threat to public health and safety, I have determined that the NRC lacks reasonable assurance that site characterization and decontamination of the Bloomsburg facility will be initiated and completed in an orderly and timely fashion to assure that the health and safety of the public, including current employees and adjoining landowners, will be protected. This is particularly so in light of the apparent financial inability of any one successor corporation to U. S. Radium to cleanup the Bloomsburg facility. Accordingly, the public health, safety and interest require that the actions required by Section VI of this Order commence immediately. For these reasons and pursuant to 10 CFR 12.201(c), no prior notice is required, and this order should be made immediately effective.

VI.

In view of the foregoing, and pursuant to Sections 81, 161b, 161i, 184 and 186 of the Atomic Energy Act of 1954, as amended, and the Commission's regulations in 10 CFR 2.204 and 10 CFR Part 30, IT IS HEREBY ORDERED, EFFECTIVE IMMEDIATELY, THAT LICENSE NOS. 37-00030-02, 08, 07E, 09G and 10G ARE MODIFIED AS FOLLOWS:

1. The following companies are named on the above licenses and subject to all liabilities under those licenses: Safety Light Corp., USR Industries, Inc., USR Lighting, Inc., USR Chemical, Inc., USR Metals, Inc., USR Natural Resources, Inc., Metreal, Inc., Pinnacle Petroleum, Inc., and all

other successor corporations to, or subsidiaries of, either U.S. Radium Corp. or USR Industries, Inc.

2. Within 90 days from the date of this Order, access shall be controlled to all contaminated areas at the Bloomsburg facility by a fence or other suitable means so as to create a restricted area, as defined in 10 CFR Part 20.
3. Within 30 days from the date of this Order, all corporations set forth in Section VI.1. of this Order shall jointly submit, to the Regional Administrator, NRC, Region I, for his review and approval, a single plan to characterize the radioactivity at the Bloomsburg site. A corporate officer, not lower than the President, from each of the corporations set forth in Section VI.1. of this Order, shall certify under oath or affirmation, to the accuracy of the information contained in the site characterization plan and to the intent on behalf of the corporation to implement the Plan.
4. Within 180 days from the date the Regional Administrator approves the site characterization plan required by Section VI.3. of this Order, all corporations set forth in Section VI.1. of this Order shall jointly submit, to the Regional Administrator, NRC, Region I, for his review and approval, a single report that shall contain a complete radiological characterization of the site, with a description of the location and level of all sources of radiation and contamination. A corporate officer, not lower than the President, for each of the corporations set forth in

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6. Following the Regional Administrator's approval of the Decontamination Plan required by Section VI.5. of this Order, a corporate officer, not lower than the President, from each of the corporations set forth in Section VI.1. of this Order shall submit a monthly status report, under oath or affirmation, to the Regional Administrator of NRC Region I, stating:
 - a. The progress that has been made toward carrying out the decontamination plan during the previous 30 days. In the event that a milestone set forth in the decontamination plan submitted in response to Section VI.5. is not met during the period covered by the report,

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- c. The financial resources available during the period covered by the report, including but, not limited to, revenue, costs and expenses, net losses or profits, and sums expended on decontamination of the Bloomsburg facility.

7. No corporation named herein shall either abandon or transfer the Bloomsburg facility or any other corporate asset, of whatever kind or form, until the NRC has confirmed that a successful decontamination of the Bloomsburg facility has been completed.

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 - b. The November 11, 1983 Safety Light submittal in response to Inspection Report 83-01;
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 - d. The sale of Safety Light Corporation in May 1982.

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6. Copies of all quarterly financial statements, including but not limited to, balance sheets showing all assets and liabilities and profit and loss statements, for the four quarters prior to this Order.
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8. A listing of the names of all individuals or corporations owning at least 10% of the stock in any corporation set forth in Section VII.1. indicating each owner's address and the number of shares owned.

IX.

The Regional Administrator of Region I may modify or relax any provision of the Order or Demand for Information upon the showing of good cause.

FOR THE NUCLEAR REGULATORY COMMISSION

Hugh Thompson, Deputy Executive Director
for Nuclear Materials Safety, Safeguards,
and Operations Support

Dated at Rockville, Maryland
this day of February 1989

THIS DOCUMENT IS BEING WITHHELD
FROM PUBLIC DISCLOSURE

DOCUMENT NUMBER: XXIX-006

7

SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

Form 10-K

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF
THE SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended December 31, 1987 Commission file No. 1-8040

USR INDUSTRIES, INC.

(Exact name of registrant as specified in its charter)

Delaware

(State or other jurisdiction of
incorporation or organization)

22-2303184

(I.R.S. Employer
Identification No.)

1717 Woodstead Court, Suite 113, The Woodlands, Texas
(Address of principal executive offices)

77380

(Zip Code)

Registrant's telephone number, including area code: (713) 367-2821

Securities registered pursuant to Section 12(b) of the Act:

Title of Each Class

Name of Each Exchange
On Which Registered

Common Stock, \$1.00 par value

American Stock Exchange

Securities registered pursuant to Section 12(g) of the Act: None

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months or for such shorter period that the registrant was required to file such reports, and (2) has been subject to such filing requirements for the past 90 days.

YES xxxx NO

As of March 1, 1988 there were 994,655 shares of the Registrant's common stock outstanding, and the aggregate market value thereof held by non-affiliates was approximately \$1,251,525.

DOCUMENTS INCORPORATED BY REFERENCE

The information called for by Part III, Items 10, 11, 12 and 13 is incorporated herein by reference to the Registrant's definitive Proxy Statement to be filed in connection with the Registrant's 1988 Annual Meeting.

XXIX-007

PART I

Item 1. Business.

GENERAL DEVELOPMENT OF BUSINESS

USR Industries, Inc. (herein "Registrant" or "Industries") was established in Delaware in 1980 as a holding company to own diversified interests, including ownership through subsidiaries of assets held previously by the former United States Radium Corporation ("USRC"). In connection with the establishment of Industries, USRC was merged into a newly formed subsidiary of Industries and the respective assets and liabilities of former corporate subsidiaries of USRC were assumed by wholly owned subsidiaries of Industries. Thereafter, to more closely reflect its business as primarily a manufacturer of safety lighting products, USRC changed its name to Safety Light Corporation ("SLC") and, in 1982, Industries sold its ownership position of SLC common stock. Since formation as above, Industries has evolved pursuant to a broad corporate development strategy known as the Plan of Asset Redeployment (the "Plan").

Plan of Asset Redeployment

Pursuant to the Plan, since formation as a holding company in 1980 Industries has deployed assets towards sectors believed to offer improved growth opportunities over the long term. Under the Plan Industries has placed emphasis primarily upon the natural resources, real estate and financial services sectors and has reduced its ownership of small manufacturing operations.

An important step in redeployment of assets away from the manufacturing sector was the sale of certain net assets of USR Chemical Products, Inc. ("Chemicals") to Mitsubishi Chemical Industries Limited of Japan ("Mitsubishi"). At the time the sale was completed in 1981, Chemicals was the principal operating subsidiary of Industries and was competing in worldwide markets against companies having substantially greater financial, technical and marketing resources. Through that sale Industries deployed assets from a cyclical and capital intensive business which appeared susceptible to increasing foreign competition. During 1985 Industries substantially completed its withdrawal from the manufacturing sector through the sales of certain net assets of its remaining manufacturing subsidiaries, USR Lighting, Inc. ("Lighting") and USR Metals, Inc. ("Metals") to corporations owned by Industries' Chairman (the "Purchasing Corporations"). Such transactions were further ratified and approved by stockholders at the following Annual Meeting held March 7, 1986.

During 1981 and early 1982, Industries established an ownership interest in the financial services and real estate sectors through purchase of common stock of Boothe Financial Corporation ("BFC"), a diversified real estate and financial services concern based in San Francisco, California. The BFC ownership position was divested in late 1983 and 1984 at a profit to Industries of approximately \$1.4 million.

Natural Resources. During late 1983 Industries established a significant ownership interest in the natural resources sector through the purchase of common stock of Pinnacle Petroleum, Inc. ("Pinnacle"), a publicly held oil and gas exploration and production company based in Denver, Colorado. Since 1983 Pinnacle has substantially expanded its scope of operations by completing several corporate transactions. See "Information Concerning Pinnacle Petroleum, Inc." and "Expansion and Development of Pinnacle" below. When calculated on a book value basis as of December 31, 1987, approximately \$1.6 million, or 28% of Industries' total assets of \$5.8 million was invested in Pinnacle Common Stock.

Real Estate. Currently, Industries' corporate development strategy emphasizes primarily the acquisition of income producing real estate deemed to have potential for capital appreciation. Industries considered the possible purchase of an ownership interest in a savings institution or other financial services company. However, in view of Industries' purchase of commercial real estate during November 1987 and limited overall financial resources, no further consideration of the financial services sector is being undertaken at this time.

During 1987 Industries met its primary objectives under the Plan by the purchase, through a limited partnership of which Industries serves as general partner, of a commercial office building located in Houston, Texas. In its capacity as general partner of the limited partnership, Industries owns an initial 55.6% partnership interest, with individual limited partners, including an unrelated party and a director and officer of Industries owning the balance. All interests in the limited partnership were purchased for the same pro rata price per unit of ownership. The building, which has total office space of approximately 53,700 net rentable square feet, currently is approximately 75% leased. The building's operating income is meeting operating costs and debt service requirements on a current basis. See "Narrative Description of Business," below.

Industries is actively evaluating the purchase of other real estate interests. In view of the limited financial resources of Industries, it is anticipated that further real estate purchases, if any, will utilize a partnership with other parties adding capital to that committed by Industries so as to diversify financial risks and maximize the asset base which Industries may manage.

NARRATIVE DESCRIPTION OF BUSINESS

Industries' current operations consist primarily of the support and development of its ownership interest in real estate and of the specialty dial manufacturing business of its subsidiary Metals, and monitoring the performance of Pinnacle. Subject to its internal financial restrictions Industries continues to evaluate the possible purchase of various interests in the real estate sector, primarily interests which may offer income potential. Significant management time and corporate resources are also involved in the conduct of litigation affecting Industries. Such litigation is further described in Notes to Consolidated Financial Statements and Note 10 thereof.

Information Concerning Pinnacle Petroleum, Inc.

Pinnacle is primarily engaged in the business of oil and gas exploration, production and development, and is expanding primarily through corporate transactions. Pinnacle's exploration activities and field operations, which until 1985 were conducted on a small scale, have expanded significantly during the period from 1985 to 1988. As typical of an independent oil and gas company, Pinnacle's operations have generally included acquiring, exchanging, selling, exploring, farming in and out, developing and otherwise dealing in oil and gas properties, primarily leaseholds, working interests and overriding and royalty interests.

Expansion and Development of Pinnacle. During late 1983, Pinnacle's management anticipated worsening economic conditions in the oil and gas industry and so pursued a conservative operating stance marked by limited drilling and exploration activity. At that time, Pinnacle also formulated a general business strategy known as Pinnacle's "Plan for Corporate Development" which provides for expansion primarily through corporate transactions, including mergers, rollups and other corporate transactions. Management of Pinnacle believes that factors including continued volatility of oil and gas prices, restricted marketability of natural gas and the continuing depressed conditions in the independent industry will continue to generate corporate transactions for review and possible participation by Pinnacle.

During 1985 Pinnacle completed three corporate transactions through which Pinnacle expanded its scope of operations. Such transactions involved, respectively, the issuance by Pinnacle of redeemable preferred stock and warrants in exchange for cash and oil and gas properties, and the payment of cash and Pinnacle Common Stock to purchase common stock of two other oil and gas exploration and production companies. Due to continuing depressed conditions in the oil and gas markets, the financial and operating strengths anticipated to be achieved through these transactions have been tempered by subsequent downturns in oil and gas prices and the writedowns of Pinnacle's producing and nonproducing properties reflected in the accompanying financial statements. Also during 1985, Pinnacle purchased in excess of 50% of the common stock of Regal Petroleum, Ltd. ("Regal"), a publicly traded company. Regal is subject to the informational requirements of the securities acts and further information concerning Regal is contained in its Annual Report on Form 10-K and other public filings.

During November 1986 (a) Pinnacle stockholders approved proposals for the issuance of a new class of common stock ("Class B Common Stock") of Pinnacle which would not be publicly tradeable but would have special voting rights; and (b) the Board of Directors approved the distribution by Pinnacle of a warrant dividend ("Warrant Dividend") entitling holders of common stock ("Common Stock") to purchase additional shares of Pinnacle Common Stock at prices of \$1.35 and \$1.50 per share during periods in 1988 and 1989, respectively. Those stockholders who elected to receive the Class B Common Stock were not entitled to receive the Warrant Dividend. The Class B Common Stock can only be transferred to a limited group of related persons, but is exchangeable for Common Stock on a share-for-share basis. Holders of the Class B Common Stock vote with the holders of Common Stock on general corporate matters. As a class the holders of Class B Common Stock are

entitled to elect a majority of the Board of Directors of Pinnacle and to vote on certain extraordinary matters. Consistent with the election made by over ninety-eight percent of other Pinnacle stockholders, Industries elected to hold its ownership of publicly tradeable Common Stock. For additional information see the accompanying Notes to Consolidated Financial Statements and the public filings and reports of Pinnacle.

During early 1987 Pinnacle executed Agreements of Purchase and Sale for two additional corporate transactions in which the issuance and delivery of unregistered shares of Pinnacle Common Stock was the consideration. Such transactions were completed on March 10, 1987, with Pinnacle acquiring V-Mc Operating Company, a privately held oil and gas operating company based in Denver, Colorado and, separately, certain producing oil and gas properties in Osage County, Oklahoma. Pinnacle issued a total of 158,569 unregistered shares of Common Stock in consideration of the purchases. In addition, through a wholly owned subsidiary Pinnacle acquired certain oil and gas working interests from privately held, unaffiliated partnerships managed in San Francisco, California. The oil and gas working interests acquired are located in Oklahoma, Kansas, Wyoming and New York. The partnerships received as consideration in exchange for the working interests conveyed to Pinnacle an aggregate of 148,983 unregistered shares of Pinnacle Common Stock.

Also during 1987 Pinnacle purchased from an unaffiliated party working interests in a shallow gas property located in western New York. Pursuant to its policy of risk sharing for production and development properties, Pinnacle purchased such working interests jointly with other participants. Pinnacle purchased approximately 25.5% of the subject working interests and Regal purchased a like percentage. Pinnacle solicited participations from other parties, including persons unrelated to Pinnacle and officers or directors thereof, who purchased the balance of the working interests. All working interests were purchased by the participants on the same pro rata basis as that of Pinnacle and a Pinnacle subsidiary was selected to operate the field. All working interest owners pay the same pro rata fees to Pinnacle's operating subsidiary for the cost of operations.

Pinnacle has also advised that it is considering proposing a business combination of Pinnacle with Regal, which could include a merger or exchange offer. To date no detailed discussions have taken place concerning any such proposal.

For further information concerning Pinnacle and steps under Pinnacle's Plan for Corporate Development, see Note 2 to Industries' Notes to Consolidated Financial Statements and the Consolidated Financial Statements of Pinnacle included herewith.

Sale of Assets of USR Lighting, Inc. and USR Metals, Inc. Following the sale of certain net assets of Chemicals to Mitsubishi, Industries substantially completed its withdrawal from manufacturing activities during 1985 through the sale, effective February 13, 1985, of certain net assets of its remaining manufacturing subsidiaries, Lighting and Metals, to the Purchasing Corporations. The total purchase price was \$1,064,000 with \$400,000 paid to Industries at closing and the balance in promissory notes having scheduled payments of principal and interest through 1995.

In connection with the transactions with the Purchasing Corporations, Industries retained the investment banking group of Connecticut National Bank, Hartford, Connecticut, a subsidiary of Hartford National Corporation ("Connecticut National"), an independent financial institution of recognized stature which is familiar with the valuation of manufacturing companies. Prior to the sales, Connecticut National delivered its written opinion that consummation of the proposed transactions would be fair, from a financial point of view, to Industries and its stockholders.

At a Meeting held March 7, 1986, stockholders of Industries ratified and approved the foregoing asset sales by the affirmative vote of approximately 95% of the shares voting. It should be noted, however, that the transactions remain subject to certain conditions subsequent, including the right of the Purchasing Corporations to rescind the transactions and to be repaid in full in the event that prior to December 31, 1988, or such later date as may be agreed, counsel for the Purchasing Corporations advises that there is any question whether the assets purchased were taken "free and clear" of claims against Industries or its subsidiary corporations. The closing date for conditions subsequent may be further extended by the Board of Directors. For a description of litigation involving Industries see Notes to Consolidated Financial Statements and Note 10 thereof.

In connection with the asset sales transaction as approved by Industries' stockholders, the landlord of a former office facility refused timely consent to assignment of a lease covering such premises. On May 22, 1986 Industries instituted legal action in New Jersey Superior Court seeking a judicial determination as to the status of such lease. The landlord answered with denials, counterclaims and additional allegations of fraud, unfairness, violations of the Racketeer Influenced and Corrupt Organization Act, securities fraud and related claims and initiated parallel litigation in Federal Court. Upon motion by Industries the Superior Court granted summary judgment against the landlord on one count, ruling that the lease had not been assigned as a matter of law and remained in effect. The landlord appealed to the Appellate Division, which ruled unanimously to affirm the Superior Court judgment in favor of Industries. The landlord then petitioned the Supreme Court of New Jersey for review. On March 10, 1988 the Supreme Court denied landlord's petition. (See Notes to Consolidated Financial Statements and Note 10(g) thereof for further description of this litigation.) The Purchasing Corporation has agreed with the Registrant not to continue to request the landlord's consent to such assignment.

Lighting and Metals had been engaged respectively in the manufacture of plastic instrument panels and various custom fabricated metal products. Metals continues one manufacturing operation, the custom fabrication of specialty dials. For further discussion of the continuing operations of Metals see "Continuing Manufacturing Operations," below.

Continuing Manufacturing Operations. Metals continues to own and operate Industries' only remaining ownership position in the manufacturing sector, the custom fabrication of specialty dials. Metals' specialty dials are used as components for watches, clocks and timers for consumer and automotive applications and are marketed through direct sales and independent sales representatives. Generally, Metals' products are fabricated and marketed on a quoted fixed-price basis. The principal raw materials used by

Metals are aluminum, steel, plastics and paints. Raw materials are available from several commercial sources and in recent years Metals has experienced no significant difficulties in obtaining supplies for its ongoing business operations. Metals holds patents, trademarks or licenses as deemed advisable in connection with its activities, but does not believe that its operations are materially dependent thereon. Metals had a backlog of orders from its ongoing product line totaling \$17,500 and \$59,200 as of December 31, 1987 and 1986, respectively. Most goods on order at December 31, 1987 were for shipment in 1988.

Metals competes against a substantial number of small specialty companies, many of which have sales and financial resources exceeding those of Metals. Price, customer service and product performance are believed important in marketing products manufactured by Metals. Price competition from foreign manufacturers, particularly those exporting to the United States from Asia, has intensified in recent years. Since 1983, Metals has become dependent on sales to a limited number of customers. During 1987 sales to three customers constituted 16%, 15% and 12% of Metals' total sales volume. No other single customer accounted for more than 10% of such sales.

Substantially all product development programs of Metals' specialty dial business are sponsored by Metals at its expense. During the last three years through December 31, 1987 expenses for research, development and engineering for continuing operations, including salaries and other expenses of personnel employed on a regular basis in such work, were not material in amount.

Various activities of Metals are subject to federal, state or local regulation with regard to environmental impact. Operations conducted by Metals have received all certificates from regulatory agencies necessary to operate Metals' manufacturing equipment in the normal course of business. Currently Industries is defending litigation in which substantial claims for alleged environmental injury are being asserted against it. Such claims arise from allegations as to operations of USRC many decades ago in the era of World War I. For further discussion as to environmental regulations and litigation see Notes to Consolidated Financial Statements and Note 10 thereof.

Employees. Industries and its subsidiaries employed nine persons on a fulltime basis as of December 31, 1987. In addition, Industries regularly employs part time personnel and outside professionals who provide accounting, legal and other services.

Financial Information about Industry Segments, Foreign and Domestic Operations and Export Sales

Industries' only remaining manufacturing interest, the custom fabrication and distribution of specialty dials, had no export sales during the last three years.

Item 2. Properties.

As of the date hereof, Industries' principal offices are located at 1717 Woodstead Court, Suite 113, The Woodlands, Texas 77380. The offices consist of approximately 2,000 square feet leased from an unaffiliated party on a month-to-month basis. During April 1988 Industries will move its

offices to an office building having approximately 53,700 rentable square feet of space located at 550 Post Oak Boulevard, Houston, Texas 77027. During November 1987 Industries purchased an approximately fifty-five percent ownership interest in such building through a limited partnership. A wholly owned subsidiary of Industries serves as general partner of the limited partnership. At the request of Industries, which required additional financial participations to close the purchase, an unaffiliated person and an officer and director of Industries put up the necessary additional financing through the purchase of limited partnership interests. Such interests were purchased for the same pro rata price as was paid by Industries. See Notes to Consolidated Financial Statements and Notes 8 and 11 thereof. Industries has leased approximately 2,000 square feet of office space in that building on a three-year basis through December 31, 1990.

Metals' manufacturing facility is located within approximately 30,000 square feet of space in Bloomsburg, Pennsylvania leased under an initial five year term through 1987. Currently Metals leases approximately 10,000 square feet of such space and the balance thereof is subleased to one of the Purchasing Corporations at a price exceeding Metals' rental expense.

Upon expiration of the lease on its 23,000 square foot facility in Parsippany, New Jersey during December 1983, Lighting entered into a lease for a term of ten years for a factory and office facility in Boonton, New Jersey comprising approximately 27,000 feet. Under a sublease of the property executed in connection with the sale of certain net assets of Lighting effective February 13, 1985, the facility was subleased at rates exceeding Lighting's rental cost to one of the Purchasing Corporations for an initial six year term through February 1991. Under the sublease the subtenant is obligated to pay all rent, property taxes and other occupancy expenses previously required to be paid by Lighting under the master lease. The facility is owned by a partnership in which an officer and director of Industries holds the principal interest, which partnership did not require Lighting's obligations under the master lease to be assumed or guaranteed by Industries.

During 1980 a lease covering administrative offices in Morristown, New Jersey formerly leased by Industries and having approximately 7,000 square feet was assigned to Lighting, which subleased the premises to an unaffiliated third party for an initial term of five years with an optional five year extension which has been exercised by the subtenant.

Management of Industries and its respective subsidiaries are of the opinion that the principal properties owned or leased thereby are adequate for their present needs and are adequately protected against insurable risks customary to their respective industries.

Item 3. Legal Proceedings.

Currently Industries is defending litigation in which substantial claims for alleged environmental damages are being asserted against it. The claims arise from alleged activities of USRC in the operation of an ore processing facility in Orange, New Jersey many decades ago in the era of World War I. The plaintiff in that environmental litigation alleges also that Industries is responsible as an alleged "successor" to USRC. Various appeals, negotiations with administrative or regulatory authorities and additional litigation is pending in various stages and forums. Industries is

party to a Defense Agreement with certain insurers under which such insurers are providing certain defense costs on behalf of their insureds. For information relating to this and additional legal proceedings see Notes to Consolidated Financial Statements and Note 10 thereof.

Item 4. Submission of Matters to a Vote of Security Holders.

None.

PART II

Item 5. Market For the Registrant's Common Equity and Related Stockholder Matters.

The following table sets forth the range of sales prices for Industries' Common Stock for each quarter during the last two fiscal years. The prices shown reflect trading on the American Stock Exchange ("Amex"). With the cooperation of the Amex, during January 1988 Industries voluntarily delisted from the Amex and trading for its common stock was established on the National Automated Quotation System under the symbol "UIND".

	<u>High</u>	<u>Low</u>
<u>1987</u>		
First Quarter	\$2.25	\$1.625
Second Quarter	1.875	1.375
Third Quarter	2.25	1.25
Fourth Quarter	2.125	1.00
<u>1986</u>		
First Quarter	\$3.125	\$2.125
Second Quarter	3.375	2.625
Third Quarter	3.00	1.625
Fourth Quarter	2.00	1.625

At March 1, 1988 there were approximately 1,400 holders of record of common stock of Industries.

No cash dividends were declared or paid during the two year period ended December 31, 1987. Management believes it unlikely that Industries will pay dividends in the foreseeable future.

Item 6. Selected Financial Data.

The following selected condensed financial information has been derived from, and is qualified by reference to and should be read in conjunction with, Industries' Consolidated Financial Statements and Notes thereto included elsewhere herein, except the data relating to the fiscal years ended December 31, 1984 and 1983 which has been derived from previously published financial statements.

- - - (in thousands except per share amounts) - - -

	Years Ended December 31,				
	1987	1986	1985	1984	1983
Revenues	\$ 573	490	359	342	664
Net earnings (loss) from continuing operations	\$ (773)	(695)	(538)	(641)	281
Net earnings (loss) per share from continuing operations	\$ (.78)	(.69)	(.52)	(.61)	.24
Total assets	\$5,834	4,067	4,911	6,050	7,319
Total current liabilities	\$ 755	581	748	1,346	1,735
Long-term obligations	\$2,097	64	-	-	65
Stockholders' equity	\$2,613	3,388	4,163	4,704	5,584

Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations.

Liquidity and Capital Resources

To date Industries has funded its internal cash needs from operations; collection of accounts receivable and other current accounts as well as through asset sales; issuance of common stock; and bank borrowings from time to time. Effective December 31, 1986, Industries terminated its two defined benefit pension plans and, in connection with such terminations, recorded a receivable of approximately \$690,000 to reflect the recovery of assets in excess of the accumulated plan benefits and costs associated with plan terminations. The distribution of excess assets and collection of the receivable took place during the third quarter of 1987. With the sales of Industries' manufacturing assets and its Plan of Asset Redeployment having been substantially completed, Industries expects to look to sales of assets to meet its liquidity needs, if such are not met from current operations.

On a consolidated reporting basis as of December 31, 1987, Industries' working capital deficit was \$40,663 and the ratio of current assets to current liabilities was .9:1 versus working capital of \$261,576 and

current ratio of 1.5:1 as of December 31, 1986. Management anticipates that during 1988 Industries may require additional sources of liquidity. To meet its liquidity requirements or in connection with other corporate objectives Industries may sell assets, offer additional securities or incur additional indebtedness.

In addition to usual transactional and operating costs, Industries has been required to bear very substantial administrative and legal expenses for certain environmental litigation. For further discussion as to environmental regulations and litigation see Notes to Consolidated Financial Statements and Note 10 thereof. Under a Defense Agreement dated September 30, 1985 to which Industries, SLC and five primary insurance carriers are parties, certain of Industries' ongoing legal defense costs in the environmental litigation have been assumed by such insurance carriers. However, the Defense Agreement does not fully cover either the direct or indirect costs to Industries of the litigation. Further, it should be noted that the insurance carriers are defending "under reservation" of their absolute right to deny all liability on the underlying claims.

Industries is subject to additional environmental claims which are not covered by any defense agreement with insurers, although negotiations for the possible participation by certain insurance carriers are in progress. Of course there can be no assurance that such discussions will result in any agreement as to defense costs. In the event that no agreement is reached with insurers with respect to such defense costs, Industries will be required to provide for additional legal expenses. Potential sources of liquidity for Industries include sales of the Common Stock of Pinnacle and discounting of notes receivable from the Purchasing Corporations.

Industries anticipates that during 1988 it may bolster its liquidity by offering its stockholders the right to purchase certain shares of Pinnacle Common Stock.

Results of Operations

1987 compared with 1986. Total revenues during 1987 increased to \$573,295 from \$490,331 in 1986. Manufacturing sales for the year ended December 31, 1987 were \$367,446 compared to \$337,631 for the comparable prior year. The increase of \$29,815 is primarily attributable to increased prices and unit sales volume. Interest income of \$61,517 for the current year, derived primarily from notes receivable from the sales of certain net assets of Lighting and Metals, increased \$6,805 from the prior year.

Cost of sales for the current year was \$140,171 compared to \$186,637 for the year ended December 31, 1986. Decreased cost of sales primarily reflect a reduction in direct labor costs. Selling, general and administrative expenses for the year ended December 31, 1987 were \$579,822 compared to \$462,417 for the prior year. The increase reflects nonrecurring expenses in connection with the purchase and operations of the office building at 550 Post Oak Boulevard, Houston, Texas 77027 offset by continued reductions in corporate overhead expenses. Industries' expenses for 1986 are net of reimbursement of certain prior costs made by five primary insurance

carriers pursuant to a Defense Agreement dated September 30, 1985. Interest expense for the current year increased \$46,823 from \$23,891 reflecting interest expense for approximately two months on the mortgage assumption connected with the office building purchase.

Effective December 31, 1986 Industries terminated its two defined benefit pension plans and a receivable of \$690,000 was recorded to reflect the recovery of assets in excess of the accumulated plan benefits and costs associated with plan terminations. Such receivable was collected in full during the third quarter of 1987.

Industries' equity in the net loss of Pinnacle of \$352,686 reflects Industries' pro rata share of Pinnacle's results of operations for 1987. The decrease from 1986 is due primarily to Pinnacle not incurring any further writedowns of its producing oil and gas properties during 1987. The management of Industries is of the opinion that oil and gas prices and markets are unlikely to decline further during 1988. In addition, Industries recorded a \$192,000 writedown on shares of Pinnacle Common Stock anticipated to be offered by Industries to its stockholders through a rights offering to be made during 1988.

Primarily as a result of the foregoing factors Industries reported a net loss of \$773,568 for 1987.

1986 Compared With 1985. Total revenues during 1986 increased to \$490,331 from \$358,826 in 1985. Manufacturing sales for the year ended December 31, 1986 were \$337,631 compared to \$246,411 for the comparable prior year. The increase of \$91,220 is primarily attributable to increased unit sales volume. Interest income of \$54,712 for 1986, derived primarily from notes receivable from the sales of certain net assets of Lighting and Metals, decreased \$7,132 from the prior year.

Cost of sales for 1986 was \$186,637 compared to \$139,132 for the year ended December 31, 1985. Increased cost of sales resulted from increased sales volume during 1986 compared to the prior year. Selling, general and administrative expenses for the year ended December 31, 1986 were \$462,417 compared to \$342,710 for the prior year. Industries' expenses for 1985 are net of reimbursement of certain prior costs made by five primary insurance carriers pursuant to a Defense Agreement dated September 30, 1985. Interest expense for 1986 decreased \$16,134 to \$23,891, reflecting lower interest rates during the year.

Industries made no sales of Pinnacle Common Stock during 1986 and realized no gain or loss therefrom during 1986. During 1985 a loss of \$67,905 was realized in connection with the sale of Pinnacle Common Stock. Effective December 31, 1986 Industries terminated its two defined benefit pension plans and a receivable of \$690,000 was recorded to reflect the estimated net reversion to Industries of surplus assets of such pension plans.

Industries' equity in the net loss of Pinnacle of \$1,110,654 reflects Industries' pro rata share of Pinnacle's results of operations for

1986. During 1986 Pinnacle's results were adversely affected by the continuation of lower oil and gas prices and writedowns of its oil and gas properties. There were no losses from discontinued operations for 1986 compared to a loss of \$19,057 in 1985. The loss for discontinued operations in 1985 reflect approximately six weeks of manufacturing operations through February 13, 1985.

The 1986 loss of \$695,468 is higher than the loss of \$557,411 sustained in 1985, primarily as a result of an increased equity pickup of \$903,001 in the net loss of Pinnacle offset by a gain of \$690,000 recognized on termination of two defined benefit pension plans.

Inflation and Changes in Prices

In recent years Industries' ownership interest have operated in sectors having generally deflationary economic environments. The impact of inflation on the revenues and expense levels reported by Industries during the past three years has been insignificant. In the event that domestic inflationary pressures reoccur management believes that Industries' ownership interests in the real estate and natural resources sectors, which traditionally have been viewed as hedges against inflation, will be relatively well positioned to adjust for inflation and changes in prices. Management expects that oil and gas prices may trend upwards during 1988 but of course no assurance can be offered as to such trends. With easing of inflationary pressures during recent years, both the selling prices for Industries' manufactured products and the costs of production, including costs of labor and materials, have tended to stabilize. However, despite declines in the U.S. dollar relative to most Asian currencies during 1987, competition in Metals' business from Asian based exporters remains intense.

Financial Accounting Standards Board's ("FASB") Statement Release

The FASB issued a Statement of Financial Accounting Standards ("SFAS") No. 96 "Accounting for Income Taxes" in December 1987. The SFAS requires substantial changes in the method of accounting for deferred income taxes and must be adopted by Industries beginning in 1989. Industries has no deferred taxes recorded and is currently in a net operating loss carryforward position. Industries has not yet adopted SFAS No. 96 and, accordingly, the impact on Industries' financial condition and results of operations has not been determined; however, Industries does not expect it to have a material adverse effect.

Item 8. Financial Statements and Supplementary Data.

Index to Financial Statements and Related Schedules	Page
USR INDUSTRIES, INC.	
Report of Independent Certified Public Accountants.....	17
Consolidated Financial Statements:	
Consolidated Balance Sheets as of December 31, 1987 and 1986.....	18
Consolidated Statements of Operations for the years ended December 31, 1987, 1986 and 1985.....	20
Consolidated Statements of Stockholders' Equity for the years ended December 31, 1987, 1986 and 1985.....	22
Consolidated Statements of Changes in Financial Position for the years ended December 31, 1987, 1986 and 1985.....	23
Notes to Consolidated Financial Statements.....	26
<u>Financial Statement Schedules</u>	
Schedule II Amounts Receivable From Related Parties and Underwriters, Promoters and Employees Other Than Related Parties.....	46
Schedule VIII Valuation and Qualifying Accounts.....	47
Schedule IX Short-Term Borrowings.....	48
Schedule X Supplementary Income Statement of Operations.....	49
PINNACLE PETROLEUM, INC.	
Report of Independent Certified Public Accountants.....	50
Consolidated Financial Statements:	
Consolidated Balance Sheets as of December 31, 1987 and 1986.....	51
Consolidated Statements of Operations for the years ended December 31, 1987, 1986 and 1985.....	53

- Continued -

Index to Financial Statements and Related Schedules (Continued)

	<u>Page</u>
Consolidated Statements of Stockholders' Equity for the years ended December 31, 1987, 1986 and 1985	54
Consolidated Statements of Changes in Financial Position for the years ended December 31, 1987 1986 and 1985.....	56
Notes to Consolidated Financial Statements.....	59
<u>Financial Statement Schedules</u>	
Schedule V Property and Equipment.....	69
Schedule VI Accumulated Depreciation, Depletion and Amortization of Property and Equipment.....	70
Schedule VIII Valuation and Qualifying Accounts.....	71
Schedule X Supplementary Income Statement Information.....	72

All other schedules are omitted since the information required thereunder is not applicable, the amounts in question are below the minimum required for presentation in a schedule or because such information is included in the consolidated financial statements and notes thereto.

REPORT OF INDEPENDENT CERTIFIED PUBLIC ACCOUNTANTS

To the Board of Directors and
Stockholders of USR Industries, Inc:

We have examined the consolidated financial statements and the financial statement schedules of USR Industries, Inc. and subsidiaries as listed in the index on pages 15 and 16 of this Form 10-K. Our examinations were made in accordance with generally accepted auditing standards and, accordingly, included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

As discussed in Note 10 to the consolidated financial statements, there exists certain litigation, the outcome of which cannot presently be determined.

In our opinion, subject to the effects on the financial statements of such adjustments, if any, as might be required had the outcome of the uncertainties referred to in the preceding paragraph been known, the consolidated financial statements referred to above present fairly the financial position of USR Industries, Inc. and subsidiaries as of December 31, 1987 and 1986 and the results of their operations and the changes in their financial position for each of the three years in the period ended December 31, 1987, in conformity with generally accepted accounting principles applied on a consistent basis. In addition, the financial statement schedules referred to above, when considered in relation to the basic financial statements taken as a whole, present fairly the information required to be included therein.

Cooper & Lybrand

Houston, Texas
March 29, 1988

USR INDUSTRIES, INC.

Consolidated Balance Sheets

	December 31, 1987	December 31, 1986
<u>ASSETS</u>		
Current assets:		
Cash and equivalents	\$ 81,646	56,079
Accounts receivable:		
Trade	69,139	60,700
Pension termination	-	690,000
Other	21,185	4,543
Inventories	27,239	19,399
Note receivable-current portion	8,860	8,185
Common stock held for sale-Pinnacle Petroleum, Inc.	500,000	-
Prepaid expenses and other	<u>5,999</u>	<u>3,556</u>
Total current assets	<u>714,068</u>	<u>842,462</u>
Ownership of common stock-Pinnacle Petroleum, Inc.	1,138,234	2,139,086
Note receivable-Purchasing Corporations	474,762	461,627
Property, plant and equipment, at cost	4,610,576	1,688,390
Less accumulated depreciation	<u>(1,214,992)</u>	<u>(1,153,095)</u>
	<u>3,395,584</u>	<u>535,295</u>
Other assets	<u>111,547</u>	<u>88,868</u>
	<u>\$5,834,195</u>	<u>4,067,338</u>

- Continued -

USR INDUSTRIES, INC.

Consolidated Balance Sheets (Continued)

	December 31, 1987	December 31, 1986
<u>LIABILITIES AND STOCKHOLDERS' EQUITY</u>		
Current liabilities:		
Notes payable and current maturities of long-term debt	\$ 216,055	230,000
Accounts payable	394,040	214,410
Accrued expenses	<u>144,636</u>	<u>136,476</u>
Total current liabilities	<u>754,731</u>	<u>580,886</u>
Other long-term liabilities	28,422	-
Deferred income	-	34,679
Long-term debt	2,005,957	-
Long-term obligation under capital lease	62,822	63,515
Minority interest - Partnership	369,123	-
Commitments and contingencies		
Stockholders' equity:		
Common stock, par value \$1; 3,500,000 shares authorized; issued and outstanding 994,655 shares at December 31, 1987 and 995,655 shares at December 31, 1986	994,655	995,655
Additional paid-in capital	365,461	366,011
Retained earnings	<u>1,253,024</u>	<u>2,026,592</u>
Total stockholders' equity	<u>2,613,140</u>	<u>3,388,258</u>
	<u>\$5,834,195</u>	<u>4,067,338</u>

See Notes to Consolidated Financial Statements.

USR INDUSTRIES, INC.

Consolidated Statements of Operations

	Years Ended December 31,		
	1987	1986	1985
Revenues:			
Net sales	\$ 367,446	337,631	246,411
Interest income	61,517	54,712	61,844
Rental income, net	82,827	67,500	10,642
Other income	61,505	30,488	39,929
Total revenues	<u>573,295</u>	<u>490,331</u>	<u>358,826</u>
Costs and expenses:			
Cost of sales	140,171	186,637	139,132
Selling, general and administration expenses	579,822	462,417	342,710
Depreciation	81,561	86,510	99,755
Interest expense	<u>46,823</u>	<u>23,891</u>	<u>40,025</u>
Total costs and expenses	<u>848,377</u>	<u>759,455</u>	<u>621,622</u>
Gain (loss) on pension termination	10,323	690,000	-
Gain (loss) on sale of assets	5,000	(5,690)	-
Gain (loss) on sale of stock	-	-	(67,905)
Market value writedown of common stock-Pinnacle Petroleum, Inc.	(192,000)	-	-
Minority interest in net loss of Partnership	30,877	-	-
Equity in net earnings (loss) of Pinnacle Petroleum, Inc.	<u>(352,686)</u>	<u>(1,110,654)</u>	<u>(207,653)</u>
Earnings (loss) from continuing operations	(773,568)	(695,468)	(538,354)
Discontinued operations:			
Earnings (loss) from operations of discontinued businesses	<u>-</u>	<u>-</u>	<u>(19,057)</u>
Net earnings (loss)	<u>\$ (773,568)</u>	<u>(695,468)</u>	<u>(557,411)</u>

- Continued -

USR INDUSTRIES, INC.

Consolidated Statements of Operations (Continued)

	Years Ended December 31,		
	1987	1986	1985
Earnings (loss) per share:			
Earnings (loss) from continuing operations	\$ (.78)	(.69)	(.52)
Earnings (loss) from discontinued operations	<u>-</u>	<u>-</u>	<u>(.02)</u>
Net earnings (loss)	<u>\$ (.78)</u>	<u>(.69)</u>	<u>(.54)</u>
Weighted average number of common shares and common share equivalents	<u>994,954</u>	<u>1,006,776</u>	<u>1,024,586</u>

See Notes to Consolidated Financial Statements.

USR INDUSTRIES, INC.

Consolidated Statements of Stockholders' Equity

	<u>Common Stock</u>		<u>Additional</u>	<u>Retained</u>	<u>Total</u>
	<u>Shares</u>	<u>Amount</u>	<u>Paid-in</u>	<u>Earnings</u>	<u>Stockholders'</u>
			<u>Capital</u>		<u>Equity</u>
Balance at December 31, 1984	1,017,650	\$1,017,650	\$ 407,217	\$3,279,471	\$4,704,338
Net earnings (loss)	-	-	-	(557,411)	(557,411)
Issuance of common stock for exercise of option	30,000	30,000	48,600	-	78,600
Treasury stock acquisitions (par value method)	<u>(23,989)</u>	<u>(23,989)</u>	<u>(38,726)</u>	<u>-</u>	<u>(62,715)</u>
Balance at December 31, 1985	1,023,661	1,023,661	417,091	2,722,060	4,162,812
Net earnings (loss)	-	-	-	(695,468)	(695,468)
Treasury stock acquisitions (par value method)	<u>(28,006)</u>	<u>(28,006)</u>	<u>(51,080)</u>	<u>-</u>	<u>(79,086)</u>
Balance at December 31, 1986	995,655	995,655	366,011	2,026,592	3,388,258
Net earnings (loss)				(773,568)	(773,568)
Treasury stock acquisitions (par value method)	<u>(1,000)</u>	<u>(1,000)</u>	<u>(550)</u>	<u>-</u>	<u>(1,550)</u>
Balance at December 31, 1987	<u>994,655</u>	<u>\$ 994,655</u>	<u>\$ 365,461</u>	<u>\$1,253,024</u>	<u>\$2,613,140</u>

See Notes to Consolidated Financial Statements.

USR INDUSTRIES, INC.

Consolidated Statements of Changes in Financial Position

	Years Ended December 31,		
	1987	1986	1985
SOURCES OF FUNDS:			
Earnings (loss) from continuing operations	\$ (773,568)	(695,468)	(538,354)
Items not affecting working capital:			
Depreciation and amortization	81,561	86,510	99,755
Accretion of discount on note receivable	(21,995)	(19,973)	(25,817)
(Increase) decrease in ownership of Pinnacle Petroleum, Inc.	(43,834)	-	14
(Gain) loss on sale of stock	-	-	67,905
(Gain) loss on sale of assets	(5,000)	5,690	-
Market value writedown of common stock	192,000	-	-
Minority interest in net loss of Partnership	(30,877)	-	-
Equity in net loss of Pinnacle Petroleum, Inc.	<u>352,686</u>	<u>1,110,654</u>	<u>207,653</u>
Funds provided by (used for) continuing operations	<u>(249,027)</u>	<u>487,413</u>	<u>(188,844)</u>
Earnings (loss) from discontinued operations	<u>-</u>	<u>-</u>	<u>(19,057)</u>
Funds provided by (used for) operations	(249,027)	487,413	(207,901)
Issuance of common stock for exercise of option	-	-	78,600
Limited partners capital contribution	400,000	-	-
Payments and current maturities of note receivable	8,860	38,785	12,853
Reclassification to common stock held for sale	500,000	-	-
Proceeds from sale of stock	-	-	300,000
Increase in notes payable	2,047,535	-	-
Increase in long-term lease obligations	-	63,515	-
Increase in deferred income	-	34,679	-
Increase in long-term liabilities	28,422	-	-
Proceeds from sale of assets	5,000	8,850	-
Net book value of non-current assets of discontinued operations	-	-	464,040
Decrease in other assets	-	49,756	30,326
Decrease in working capital	<u>302,239</u>	<u>-</u>	<u>-</u>
	<u>\$3,043,029</u>	<u>682,998</u>	<u>677,918</u>

- Continued -

USR INDUSTRIES, INC.

Consolidated Statements of Changes in Financial Position (Continued)

	Years Ended December 31,		
	1987	1986	1985
• USES OF FUNDS:			
Additions to property, plant and equipment, net	\$2,941,850	96,790	1,643
Increase in other assets	22,679	-	-
Current maturities of long-term lease obligations	693	-	-
Payments and current maturities of notes payable	41,578	-	-
Increase in note receivable	-	-	467,475
Decrease in deferred income	34,679	-	-
Treasury stock acquired	1,550	79,086	62,715
Increase in working capital	-	507,122	146,085
	<u>\$3,043,029</u>	<u>682,998</u>	<u>677,918</u>

- Continued -

USR INDUSTRIES, INC.

Consolidated Statements of Changes in Financial Position (Continued)

	Years Ended December 31,		
	1986	1985	1984
CHANGES IN COMPONENTS OF WORKING CAPITAL:			
Increase (decrease) in current assets:			
Cash and equivalents	\$ 25,567	35,923	(80,007)
Accounts receivable	(664,919)	301,277	28,589
Inventories	7,840	5,656	(268)
Note receivable	675	623	7,562
Common stock held for sale- Pinnacle Petroleum, Inc.	500,000	-	-
Prepaid expenses and other	2,443	(3,471)	(4,437)
Net assets of discontinued businesses held for sale	-	-	(403,435)
	<u>(128,394)</u>	<u>340,008</u>	<u>(451,996)</u>
Increase (decrease) in current liabilities:			
Notes payable and current maturities of long-term debt	(13,945)	-	(300,000)
Accounts payable	179,630	(156,944)	29,860
Accrued expenses	<u>8,160</u>	<u>(10,170)</u>	<u>(327,941)</u>
	<u>173,845</u>	<u>(167,114)</u>	<u>(598,081)</u>
Increase (decrease) in working capital	<u>\$ (302,239)</u>	<u>507,122</u>	<u>146,085</u>

See Notes to Consolidated Financial Statements.

USR INDUSTRIES, INC.

Notes to Consolidated Financial Statements

(1) SUMMARY OF SIGNIFICANT ACCOUNTING PRINCIPLES

Principles of Consolidation. The accompanying consolidated financial statements include the accounts of USR Industries, Inc. ("Industries") and its wholly owned subsidiaries Metal Fabricators, Inc., USR Lighting, Inc. ("Lighting"), USR Metals, Inc. ("Metals"), USR Chemicals, Inc., Unatco Funding Corporation, 550 POB, Inc. and Industries' majority owned limited partnership, Houston-Phoenix Co., Ltd. All significant intercompany accounts and transactions have been eliminated.

During 1985 in connection with various corporate transactions undertaken pursuant to its Plan for Corporate Development, Pinnacle Petroleum, Inc. ("Pinnacle") issued Convertible Voting Preferred Stock, Warrants and Common Stock. At December 31, 1985, after giving effect to the increased number of Pinnacle voting securities outstanding after such transactions, Industries' voting position was reduced to approximately 40% of Pinnacle's total voting securities then outstanding. At and subsequent to that time the consolidated financial statements of Industries present the ownership of common stock of Pinnacle under the equity method.

Inventories. Inventories of raw materials are carried at the lower of cost (first-in, first-out) or market. Work-in-process and finished goods inventories are valued at the lower of average cost or market.

Property, Plant and Equipment. Property, plant and equipment are depreciated over the estimated useful lives of the depreciable assets using the straight line method. Expenditures for maintenance and repairs which do not improve or extend the useful lives are charged to operations as incurred, while expenditures for major renewals and betterments are capitalized. Dispositions of assets are reflected at the historical costs less accumulated depreciation, with resulting gain or loss reflected in operations currently.

Federal Income Taxes. Industries and its wholly owned subsidiaries join in filing a consolidated federal income tax return. Investment tax credits are accounted for by the flow-through method.

Accruals and Reserves. The consolidated financial statements include a provision to the statement of operations established for the year ended December 31, 1983 for estimated future litigation expenses in connection with claims asserted against Industries and its wholly owned subsidiaries. The accrual of \$100,000 remains on the Consolidated Balance Sheets as of December 31, 1987 and 1986 with respect to such expenses. See Note 10.

Earnings Per Share. Net earnings (loss) per share of common stock are based on the weighted average number of shares of common stock and common stock equivalents from stock options. Exercise of options outstanding at

USR INDUSTRIES, INC.

Notes to Consolidated Financial Statements (Continued)

December 31, 1985 was calculated to have a dilutive effect and such options were included in the calculation of primary earnings per share using the treasury stock method. The effect of the exercise of such options on the fully diluted earnings per share was immaterial.

Financial Accounting Standards Board's ("FASB") Statement Release. The FASB issued a Statement of Financial Accounting Standards ("SFAS") No. 96 "Accounting for Income Taxes" in December 1987. The SFAS requires substantial changes in the method of accounting for deferred income taxes and must be adopted by Industries beginning in 1989. Industries has no deferred taxes recorded and is currently in a net operating loss carryforward position. Industries has not yet adopted SFAS No. 96 and, accordingly, the impact on Industries' financial condition and results of operations has not been determined; however, Industries does not expect its adoption to have a material adverse effect.

Reclassifications. Presentation of the financial statements for 1986 has been changed to conform with the 1987 financial statement classifications. Such reclassifications have no effect on results of operations as reported previously.

(2) OWNERSHIP OF SECURITIES OF PINNACLE PETROLEUM, INC.

On June 20, 1985, Industries sold 111,111 shares of Pinnacle Common Stock to Pinnacle for a net price of \$2.70 per share. Industries, which purchased such shares from Pinnacle in December 1983, realized a loss of \$67,905 on the sale after giving effect to basis adjustments since the purchase date. On the date of sale, Pinnacle Common Stock was reported in the over-the-counter market as \$1.50 bid and \$1.75 asked per share. The Chairman of Industries also serves as Chairman of Pinnacle. Also during 1985, Pinnacle issued Convertible Voting Preferred Stock, Warrants and Common Stock in connection with acquisitions. After giving effect to the increased number of shares of Common and Preferred Stock issued in connection with such transactions, at December 31, 1985 Industries' voting position was reduced to approximately 40% of Pinnacle's total voting securities then outstanding and is accounted for under the equity method.

At Pinnacle's 1986 Annual Meeting, stockholders approved a Class B Proposal (the "Proposal") pursuant to which stockholders could elect on a "one-time only" basis to exchange shares of Pinnacle Common Stock, on which a Warrant Dividend had been declared under the Proposal, for shares of Class B Common Stock on a share-for-share exchange. The Class B Common Stock has the right to elect a majority of Pinnacle's Board of Directors and certain other greater voting rights, but was not eligible to receive the Warrant Dividend and is not freely tradeable. So as to receive the Warrant Dividend, which was distributable only to holders of the fully marketable Common Stock, Industries elected to continue to hold its shares of Common Stock. Upon distribution of the Warrant Dividend, Industries received a total of 205,759 Warrants from Pinnacle, with each Warrant entitling the holder to purchase

USR INDUSTRIES, INC.

Notes to Consolidated Financial Statements (Continued)

one share of Common Stock of Pinnacle, subject to postponement in certain events. Subject to certain conditions Warrants are exercisable from April 1, 1988 until May 31, 1988 and from April 1, 1989 until May 31, 1989 at exercise prices of \$1.35 per share and \$1.50 per share, respectively. However, the Board of Directors of Industries has been advised that the initial exercise date will be postponed for 180 days as provided by the terms of the Warrant. Industries' ownership position in Pinnacle Common Stock represented approximately 44% of the total number of shares of Pinnacle Common Stock outstanding at December 31, 1987. During 1987 Industries received an additional 29,223 shares of Pinnacle Common Stock as a result of terminating its pension plans as further discussed in Note 5. Such shares are included in Industries' ownership of Pinnacle Common Stock above.

Industries anticipates that during 1988 certain shares of Pinnacle Common Stock will be offered to its stockholders through a rights offering. Industries recorded a writedown of the book value of such shares of \$192,000 for 1987 and the adjusted amount was reclassified as a current asset at December 31, 1987.

Summarized financial information for Pinnacle is shown below. Additional information concerning Pinnacle is contained in Pinnacle's own periodic filings and Annual Reports on Form 10-K.

	December 31,	
	1987	1986
Current assets	\$ 3,513,141	4,494,277
Property and equipment, net	2,354,516	2,394,146
Other assets	78,820	-
	<u>\$ 5,946,477</u>	<u>6,888,423</u>
Current liabilities	\$ 697,118	572,994
Convertible preferred stock - redeemable	-	450,000
Minority interest - Regal Petroleum, Ltd.	1,357,049	1,560,999
Stockholders' equity	<u>3,892,310</u>	<u>4,304,430</u>
	<u>\$ 5,946,477</u>	<u>\$ 6,888,423</u>

USR INDUSTRIES, INC.

Notes to Consolidated Financial Statements (Continued)

	Years Ended December 31,		
	1987	1986	1985
Revenues	\$ 1,029,108	1,034,091	672,318
Costs and expenses	<u>2,019,019</u>	<u>4,058,364</u>	<u>1,003,405</u>
Earnings (loss) from operations	(989,911)	(3,024,273)	(331,087)
Minority interest in net loss of Regal Petroleum, Ltd.	203,950	923,560	-
Equity in net loss of Regal Petroleum, Ltd.	<u>-</u>	<u>-</u>	<u>(16,166)</u>
Net earnings (loss)	<u>\$ (785,961)</u>	<u>(2,100,713)</u>	<u>(347,253)</u>

(3) DISCONTINUED OPERATIONS

Effective February 13, 1985 certain net assets of Lighting and Metals were sold to newly formed corporations owned by the Chairman of Industries (the "Purchasing Corporations"). In connection with its review of the transaction, the Board of Directors of Industries received the written opinion of an independent financial institution that the transaction would be fair, from a financial point of view, to Industries and its stockholders. At a Meeting held March 7, 1986 Industries' stockholders approved and ratified the sales transactions.

As consideration for the net assets sold, Lighting and Metals received proceeds having a total face amount of \$1,064,000 of which \$400,000 was paid in cash at closing with the balance paid in installment notes issued by the Purchasing Corporations having an aggregate face value of \$664,000. For financial statement reporting purposes, the principal amount of such notes receivable of \$664,000 was discounted as of February 13, 1985, their date of issue, to an assumed market interest rate of 11% resulting in a discount of \$196,525 from the original face value of the notes to an adjusted principal amount of \$467,475. The terms of the notes call for principal and interest payments to be received in varying installments through March 31, 1995.

During 1987, 1986 and 1985 interest income from the notes of the Purchasing Corporations totalled \$55,045, \$53,646 and \$59,893 of which \$21,995, \$19,973 and \$25,817, respectively, were attributable to accretion of the original issue discount discussed above.

In connection with such transactions, the landlord of a small office facility leased on a long term basis by Lighting refused consent to assignment of such lease to one of the Purchasing Corporations. During May 1986 Lighting instituted legal action in New Jersey Superior Court seeking a judicial determination as to the status of the lease. The landlord answered with denials and counterclaims and instituted separate legal action in

USR INDUSTRIES, INC.

Notes to Consolidated Financial Statements (Continued)

Federal District Court. Thereupon motion for summary judgment against the landlord was made in Superior Court by Lighting and Industries. On December 19, 1986 the Superior Court granted that motion for summary judgment. In granting summary relief to Lighting and Industries, the Superior Court held that the lease had not been assigned as a matter of law, and remained in effect.

The landlord took an appeal to the Appellate Division from the Superior Court decision. During late 1987 the Appellate Division unanimously affirmed the action of the Superior Court in granting summary judgment in favor of Lighting and Industries.

The landlord then petitioned the Supreme Court of the State of New Jersey for review of the unanimous Appellate Division ruling against the landlord. By order dated March 10, 1988 the Supreme Court denied the landlord's petition. (See Note 10 and 10(g).)

During 1986 Lighting, Industries and the Purchasing Corporation mutually agreed to exclude any transfer of such lease from the transactions. Accordingly, for the year ended December 31, 1986 and thereafter the long-term obligations and related sublease income attributable to such lease continue to be presented on the consolidated financial statements of Industries.

The asset sales transactions are subject to certain conditions subsequent, including the right of the Purchasing Corporations to rescind the transactions and to be repaid the purchase price in full in the event that their counsel shall, prior to December 31, 1988, advise that there is any question whether the assets were purchased "free and clear" of claims against Industries or its subsidiaries. Such date may be further extended by mutual agreement of the parties.

(4) PROPERTY, PLANT AND EQUIPMENT

A summary of property, plant and equipment at December 31, 1987 and 1986 is as follows:

	December 31,	
	1987	1986
Buildings	\$3,120,766	183,254
Machinery and equipment	860,016	875,342
Office furniture and fixtures	70,148	70,148
Leasehold improvements	559,646	559,646
	4,610,576	1,688,390
Less accumulated depreciation	(1,214,992)	(1,153,095)
	<u>\$3,395,584</u>	<u>535,295</u>

USR INDUSTRIES, INC.

Notes to Consolidated Financial Statements (Continued)

(5) PENSION PLANS

In 1985 and 1986, Industries and its wholly owned subsidiaries had two pension plans which covered substantially all hourly and salaried employees. Industries made annual contributions to the plans equal to the amounts accrued for pension expense and based on actuarial determination. Pension expense included amortization of past service costs over a maximum of 40 years. During 1985 and 1986 Industries incurred no pension expense as the plans were fully funded.

Effective December 31, 1986 the foregoing defined benefit pension plans were terminated. In connection with the termination, Industries recorded a receivable of \$690,000 in its consolidated financial statements at December 31, 1986 to reflect the estimated recovery of assets in excess of the accumulated plan benefits and costs associated with plan terminations. During the third quarter of 1987 such receivable was collected in full.

Effective January 1, 1987, Industries adopted a 401(k) savings plan. The plan covers all employees who have completed one or more years of service and are not covered by a collective bargaining agreement. Each participant may make annual contributions up to the lesser of \$7,000 or 13% of compensation. Industries, at its discretion, may match a participant's contribution up to 2% of compensation. Participant contributions are vested at all times, and the discretionary employer contributions vest 20% per year after two years. Industries incurred no contribution expense in 1987. Additionally, effective January 1, 1987 Industries adopted a defined benefit plan for all employees covered by a collective bargaining agreement. Industries' annual contribution to the plan is actuarially determined. Participants in the plan are fully vested after five years of service. The actuarial status of the defined benefit plan at December 31, 1987 has not been determined; however, management does not consider the impact of the plan to be material to the consolidated financial statements.

(6) FEDERAL INCOME TAXES

For federal income tax purposes at December 31, 1987 Industries and its wholly owned subsidiaries had net operating loss carryforwards of approximately \$436,000 which expire at various dates through the year 2002 and investment tax credit carryforwards of approximately \$28,700 which expire through the year 2000.

For financial reporting purposes at December 31, 1987 Industries and its wholly owned subsidiaries had \$2,729,000 of net operating loss carryforwards and approximately \$5,600 of net investment tax credit carryforwards. Certain items of income and expense, primarily depreciation, are recognized for income tax purposes in amounts and periods which differ from those recognized for financial reporting purposes. Investment tax credit carryovers have been reduced in accordance with the Tax Reform Act of 1986.

USR INDUSTRIES, INC.

Notes to Consolidated Financial Statements (Continued)

(7) COMMON STOCK

At a Meeting held on June 13, 1984 stockholders of Industries adopted an Employees' Incentive Stock Option Plan covering 50,000 shares of Common Stock. On December 27, 1984 the Board of Directors approved the grant of an option to an officer of Industries covering 30,000 of such shares exercisable at any time in whole or in part through December 26, 1989 at a price of \$2.62 per share. The exercise price was equivalent to 110% of the closing price of Industries' Common Stock on the American Stock Exchange as of the date of grant. During 1985 that officer exercised such option in full and paid to Industries a total of \$78,600.

Where its overall business objectives and current liquidity position permit, Industries may purchase its Common Stock in open market or private transactions from time to time. Subject to the availability of funds, market conditions and other factors Industries may make purchases in the future. Treasury stock is recorded on the par value method.

(8) LEASES

Industries' principal offices are located at 1717 Woodstead Court, Suite 113, The Woodlands, Texas 77380. The offices consist of approximately 2,000 square feet leased from an unaffiliated party on a month-to-month basis. During April 1988 Industries will move its offices to the office building in which Industries has acquired a substantial ownership interest, further described at Note 11. That building is located at 550 Post Oak Boulevard, Houston, Texas 77027, and has approximately 53,700 net rentable square feet. Industries has leased approximately 2,000 square feet of office space on a three-year lease through December 31, 1990.

Industries' wholly owned subsidiary, Lighting, leases an office building and a manufacturing facility under long-term capital and operating leases, respectively. The leases contain varying terms and renewal options. Both facilities leased by Lighting are subleased at rentals in excess of their lease expense. Industries did not itself guarantee any obligation under the operating lease.

USR INDUSTRIES, INC.

Notes to Consolidated Financial Statements (Continued)

At December 31, 1987, the aggregate future minimum lease payments under the capital lease and Lightings' noncancellable operating lease are as follows:

	Capital Lease	Operating Lease
1988	\$ 5,318	\$127,000
1989	5,318	127,000
1990	5,318	127,000
1991	5,318	127,000
1992	5,318	127,000
Subsequent to 1992	<u>130,303</u>	
Total minimum lease payments	156,893	
Less amount representing interest	<u>(93,378)</u>	
Present value of future minimum lease payments	63,515	
Less current obligation	<u>(693)</u>	
	<u>\$ 62,822</u>	

Total rental expense on the operating lease was approximately \$127,000 for each of the years ended December 31, 1987, 1986 and 1985. Sublease rental income under the operating lease for the years ended December 31, 1987, 1986 and 1985 was approximately \$166,000, \$194,000 and \$111,000, respectively from the Purchasing Corporations. Future sublease rental income under current sublease contracts respecting the operating and capital leases is scheduled to be approximately \$662,000. For financial reporting purposes, sublease rental income is recorded net of rental expense.

In connection with its acquisition of the office building, Houston-Phoenix Co., Ltd., the limited partnership which purchased the building (the "Partnership"), has leased office space to tenants under various operating leases. At December 31, 1987 future minimum lease payments to be received from such operating leases are as follows:

Years Ended December 31,

1988	\$ 407,353
1989	424,098
1990	366,729
1991	142,441
1992	<u>5,639</u>
	<u>\$1,346,260</u>

Options for renewals exist ranging in terms from three to five years and in rates from \$13.00 per square foot to 95% of the prevailing base rental for like space but not less than \$10.50 per-square foot.

USR INDUSTRIES, INC.

Notes to Consolidated Financial Statements (Continued)

(9) NOTES PAYABLE AND LONG-TERM DEBT

Notes payable and long-term debt at December 31, 1987 consisted of the following:

	December 31, 1987
Commercial bank note	\$ 180,000
Mortgage note	1,942,012
Notes to limited partners	<u>100,000</u>
	2,222,012
Less current maturities	<u>(216,055)</u>
	<u>\$2,005,957</u>

The commercial bank loan, which is collateralized by shares of Common Stock of Pinnacle, bears interest at the rate of prime plus 2% (8.75% at December 31, 1987) and matures on September 30, 1988. The mortgage note payable bears an interest rate of 9.625% and is collateralized by the office building. The mortgage note is due in monthly installments of \$18,371 which include principal and interest with the balance of \$1,502,683 due in August 1996. The notes to limited partners bear interest at 8% per annum with interest due annually and principal due at the earlier of December 31, 1997 or the substantial disposition of the assets of the Partnership. These notes are collateralized by the general partners' interest in the Partnership. Scheduled maturities at December 31, 1987 for each of the five years through December 31, 1992 are \$216,055, \$38,582, \$42,463, \$46,736 and \$51,438, respectively.

(10) COMMITMENTS AND CONTINGENCIES

Legal Proceedings

(a) On April 2, 1981 an action was commenced in the Superior Court of New Jersey, Essex County, by T & E Industries, Inc. naming USRC, the corporate predecessor to Safety Light Corporation ("SLC"), as a defendant and alleging, inter alia, that property in Orange, New Jersey owned by the plaintiff suffers from contamination from certain radioactive materials allegedly deposited thereon by USRC during prior years. The litigation arises from operations conducted by USRC at the site during the years 1917 to 1926. Subsequent to the commencement of this action the complaint was amended to include Industries and certain of its subsidiaries alleged to be corporate successors to the former USRC. The plaintiff seeks to compel remedial action as to alleged improper condition of the site and damages in unspecified amounts in compensation for injury to its property and business as well as punitive damages.

USR INDUSTRIES, INC.

Notes to Consolidated Financial Statements (Continued)

During December 1983 plaintiffs amended such complaint to include as additional defendants GAF Corporation, Mitsubishi Chemical Industries, Inc. ("MCI") and MCI's subsidiary in New Jersey, USR Optonix, Inc., which was alleged to be a corporate successor to the former USRC. The additional defendants were claimed to be liable under the product line exception to the general theory that a third party purchaser of assets is not liable as a successor. The additional defendants answered denying liability and demanded that the previously named defendants defend the action on their behalf and indemnify them against costs and any potential liability in connection therewith. In 1984 the additional defendants were successful on a motion for summary judgment against the plaintiffs and, accordingly, the claims of the additional defendants against Industries and its subsidiaries have been dismissed.

In early 1985 Industries prevailed against a motion for summary judgment by the plaintiff seeking judgment that Industries is the successor to USRC.

In September 1985 five primary insurance carriers of Industries and SLC assumed the defense of Industries, certain of Industries' subsidiaries and SLC, pursuant to a Defense Agreement. While the insurance carriers are assisting in the defense of certain actions their defense is made subject to an absolute reservation of rights to deny liability on any of the underlying claims.

On February 3, 1986, this matter was tried before a jury in front of the Honorable Stanley G. Bedford. This trial was only with respect to the liability, if any, of SLC. Prior to trial, the Court bifurcated the count asserting liability against Industries and certain of Industries' subsidiaries and on November 18, 1985 ordered that all claims against Industries would be severed and separately tried, if at all, in the event plaintiff obtains a judgment against SLC.

During trial the Court granted a directed verdict in favor of SLC dismissing all of plaintiff's strict liability claims, all negligence based claims relating to the conduct of USRC between 1917-1926, and all claims based upon fraud, recklessness and intentional conduct. The only remaining claims against SLC were an alleged negligent failure to warn when the premises were sold in 1943 and a negligence theory which allegedly placed upon USRC a continuing duty to warn prospective purchasers up through the time plaintiff purchased the property in 1974, thirty-one years later. The Court also reduced plaintiff's damage claim from \$2.8 million to under \$400,000.

On March 11, 1986, the jury returned a verdict, finding that USRC was not negligent in 1943 when it failed to warn its immediate purchaser that the presence of radioactive tailings on the premises constituted a potential risk to health or property. The jury did find that USRC was negligent for not warning plaintiff before its purchase of the property thirty-one years

USR INDUSTRIES, INC.

Notes to Consolidated Financial Statements (Continued)

later, in 1974, that the same potential risk to health or property existed on the premises. Damages were assessed against SIC in the amount of \$372,100.62.

On April 25, 1986, Judge Bedford granted SIC's motion for judgment in its favor notwithstanding the jury's verdict of March 11, 1986. The Court also denied plaintiff's application for indemnification by SIC of all cleanup costs assessed against plaintiff as a result of any future government efforts to decontaminate the property. Final judgment was thereafter entered in favor of SIC, Industries and certain of Industries' subsidiaries on May 29, 1986 and awarded on June 20, 1986, dismissing all of plaintiff's claims in their entirety.

On July 9, 1986, plaintiff filed a Notice of Appeal from the June 20, 1986 judgment. On February 24, 1988 oral argument on plaintiff's appeal was heard by the Appellate Division of the State of New Jersey. No prediction can be made concerning the outcome of such argument on appeal or when the three-court panel of the Appellate Division may render its decision.

Since plaintiff's claims against Industries and certain of Industries' subsidiary companies will only be litigated in the event plaintiff is ultimately successful in its appeal against SIC, it is unclear at this time when, if at all, such claims will be tried. If a trial against Industries and certain of its subsidiaries does occur there remains to be resolved the outstanding issues of indemnification by SIC and crossclaims between it and Industries.

Claims also were made by T & E Industries in an action brought in the U.S. District Court for the District of New Jersey, allegedly pursuant to the Comprehensive Environmental Response, Compensation Liability Act of 1980 ("CERCLA") seeking a declaration that defendants are liable for all costs of cleanup and decontamination, consistent with the National Contingency Plan, of the site presently known as 422 Alden Street, Orange, New Jersey and seeking a judgment for "response costs" already incurred and injunctive relief for enforcing such remedy. Defendants made a motion to dismiss and plaintiffs made a cross-motion for partial summary judgment against SIC. The motions were heard on February 10, 1988. The Court, through Judge Wolin, found against the defendants' motion to dismiss based on New Jersey's "entire controversy doctrine" and granted T & E's application that SIC is liable under CERCLA for all necessary costs of response incurred by T & E which are consistent with the National Contingency Plan. The Court, however, limited T & E's alleged damages and determined, inter alia, that T & E's claim for attorney's fees are not recoverable response costs under CERCLA. Defendants are considering filing a petition with the Federal District Court to have the issue involving the entire controversy doctrine certified to the Third Circuit. No such petition has been filed to date.

At this time, neither counsel nor management can predict the outcome of the litigation.

USR INDUSTRIES, INC.

Notes to Consolidated Financial Statements (Continued)

(b) On December 6, 1982 an action was commenced in the Superior Court of New Jersey, Essex County, by Leslie Zwain et al. naming as defendants SLC, Industries and certain of Industries' subsidiaries alleged to be corporate successors to the former USRC and claiming, inter alia, that because of alleged contamination of the site in Orange, New Jersey, described in (a) above, the plaintiffs have suffered business interruption, diminution of property values, mental anguish and loss of consortium. The plaintiffs seek compensatory and punitive damages in amounts to be established at trial.

On August 5, 1985, the Court dismissed plaintiffs' personal injury claims based upon plaintiffs' failure to institute legal action within the applicable statute of limitations period. On February 25, 1986 the Appellate Court reversed this dismissal and remanded the matter for further proceedings. Defendants' application for leave to appeal this issue to the New Jersey Supreme Court was subsequently denied.

On November 30, 1987 the forgoing action was settled.

As in the T & E Industries litigation, the same five primary insurance carriers of Industries and SLC have assumed the defense of Industries, certain of Industries' subsidiaries and SLC, with a complete reservation of their rights to deny liability on the underlying claims.

(c) During 1984 and 1985 SLC, Industries and its two manufacturing subsidiaries, USR Lighting, Inc. and USR Metals, Inc., were named as defendants in five actions commenced in Superior Court, Essex, County, New Jersey. These actions were brought on behalf of certain residents in the Townships of Montclair, Glen Ridge and West Orange, New Jersey and claim, inter alia, damages to land and personal injury in amounts to be proved at trial as well as punitive damages. Such alleged damages are claimed to have been caused by actual or threatened exposure of the property and persons of plaintiffs to levels of radon gas, a radioactive decay product of uranium or radium bearing ores, at levels above background levels naturally occurring and in excess of permissible levels established by the government for members of the public. Plaintiffs allege that such radon gas is a product of landfill obtained from the former USRC site in Orange, New Jersey.

By notice of motion returnable on July 18, 1986, Industries, certain of Industries' subsidiaries and SLC moved for summary judgment dismissing plaintiffs' claims based upon the continued lack of a factual nexus between their activities and the presence of radon in plaintiffs' homes. The motion was also based upon the inapplicability of the legal theories advanced by plaintiffs to these matters. By order dated August 22, 1986, the Court granted in part and denied in part the motion for summary judgment, ruling that there remained factual issues preventing the dismissal of certain claims which could not be resolved without a full plenary hearing. The Court dismissed all causes of action based upon manufacture of a defective product, breach of an express or implied warranty, battery and

USR INDUSTRIES, INC.

Notes to Consolidated Financial Statements (Continued)

trespass. By the same order, the Court also consolidated these matters for discovery and trial purposes.

By order dated January 16, 1987, the Court granted the motion filed by Industries, certain of Industries' subsidiaries and SLC for severance and separate trial of certain liability and damage issues. The Court directed that these matters be tried in three separate phases: (1) a Phase I trial relating solely to plaintiffs' claims that the allegedly contaminated soil around plaintiffs' homes originated at the former USRC site in Orange, New Jersey; (2) if plaintiffs are successful in the Phase I trial, a second trial would follow encompassing all remaining liability issues; and (3) if plaintiffs are successful again in the Phase II trial, a third trial would follow relating to plaintiffs' personal injury and property damage claims.

On November 19 and 20, 1987 the defendants' motion for partial summary judgment regarding the absence of contaminated soil originating from the Orange site of the former USRC on plaintiffs' property was argued before the Superior Court of New Jersey, Law Division, Essex County. By letter opinion dated January 28, 1988, as supplemented by Judge Yanoff's letter of February 4, 1988, the Court granted-in-part and denied-in-part defendants' application. The Court adjudicated as a fact that there is no contaminated fill originating from the Orange site on six of the properties claiming to be contaminated and directed a hearing, with further expert testimony, regarding the alleged presence of contaminated sub-surface material on 14 properties as well as 30 remaining properties where certain bore hole sampling results were relied upon. On March 18, 1988, the Court denied plaintiffs' request for a rehearing on defendants' motion, as well as plaintiffs' request for leave to perform additional bore hole sampling and analysis to oppose defendants' application. The Court directed that within 90 days, plaintiffs are to provide defendants with a report from each expert plaintiffs intend to produce at the aforesaid hearing. Defendants will have 30 days from the receipt of same to submit a report from each expert, if any, defendants intend to produce at the hearing. A date for that hearing has not yet been set by the Court.

Based upon the current state of the law and the absence of evidence indicating that the activities of Industries or its subsidiaries are in any way related to the alleged presence of radon in and around plaintiffs' homes, there exist numerous defenses going to the merits in these actions.

As in the T & E Industries and Zwain matters, the same five primary insurance carriers of Industries and SLC have assumed the defense of Industries, certain of Industries' subsidiaries and SLC, with a complete reservation of rights.

At this time neither counsel nor management can predict the outcome of the litigation.

USR INDUSTRIES, INC.

Notes to Consolidated Financial Statements (Continued)

(d) On May 15, 1986, an action was commenced in the Superior Court of New Jersey, Essex County, by the Estate of Alexander F. Masson, et al. naming as defendants SLC, Industries and its two former manufacturing subsidiaries, USR Lighting, Inc. and USR Metals, Inc. This action is brought on behalf of the estate of a deceased resident of the Township of Montclair and the deceased plaintiff's brother who allege that the defendants are responsible for the presence of radon gas which was discovered in and around the deceased plaintiff's home. As with the actions identified in (c) above, plaintiffs allege that such radon gas is a product of landfill obtained from the former USRC site in Orange, New Jersey. Plaintiffs allege that the radon gas was the contributing and/or sole cause of the deceased plaintiff contracting lung cancer. Plaintiffs have also named four tobacco companies alleging that cigarettes manufactured by those defendants and smoked by the deceased plaintiff were also the contributing and/or sole cause of the deceased plaintiff contracting cancer.

Based upon the current state of the law and the absence of evidence indicating that the activities of Industries or its subsidiaries are in any way related to the alleged presence of radon in and around plaintiffs' homes, there exists numerous defenses going to the merits of this action.

As in the matters identified in (a), (b) and (c) above, the same five primary insurance carriers of Industries and SLC have assumed the defense of Industries, certain of Industries' subsidiaries and SLC, with a complete reservation of rights.

At this time neither counsel nor management can predict the outcome of the litigation.

(e) U.S. Environmental Protection Agency Proceedings

The U.S. Environmental Protection Agency ("EPA") has included the Orange, New Jersey site and the Montclair, Glen Ridge and West Orange sites on the national priorities list of the Comprehensive Environmental Response Compensation Liability Act of 1980, 42USC9601 et seq. and has notified Industries that it may be a potentially responsible party under that Act. Industries has provided requested information to the EPA. In view of the decision of Judge Wolin of the U.S. Federal District Court declaring SLC a liable party under CERCLA for the remediation and cleanup for the Orange site the defendants are contacting the EPA to inquire whether the defendants' participation in the remediation study of the Orange site being conducted by the EPA is a feasible alternative. Currently the defendants are informed that the EPA has contracted with an engineering firm regularly used by the EPA for that purpose to prepare and deliver a revised remedial investigation and study for the Orange site.

In late 1984, one of Industries' primary insurance carriers assumed the defense of Industries and certain of its subsidiaries in this potential lawsuit, while reserving its rights to disclaim liability.

USR INDUSTRIES, INC.

Notes to Consolidated Financial Statements (Continued)

(f) Proceedings Against Certain Insurers

During 1984 Industries notified its insurance carriers as to the pendency of certain of the above described actions and requested that such carriers defend and indemnify Industries as a named insured under various primary insurance policies as well as excess coverage or umbrella policies. All such carriers answered denying liability and denying any obligation to defend Industries against the claims asserted. Thereupon on August 20, 1984 Industries commenced an action in Superior Court of New Jersey, Essex County, naming as defendants all of Industries primary and excess coverage insurers and seeking judicial determination as to such carriers' duty to defend and to indemnify Industries and its subsidiaries and seeking reimbursement of costs expended by Industries for its defense, assumption of such defense on an ongoing basis, damages for wrongful declination to defend and punitive damages and counsel fees for willful failure to defend and indemnify Industries in each of the foregoing actions.

In September 1985, five primary insurance carriers of Industries and SLC assumed the defense of Industries and certain of its subsidiaries alleged to be successors in certain of the underlying actions described above, while reserving their right to disclaim liability. As a result of that Agreement, this action has been stayed except with respect to applications by plaintiffs to require other primary insurance carriers not party to the Defense Agreement to provide for a defense indemnification of Industries, certain of Industries' subsidiaries and SLC.

While there can of course be no assurance as to the outcome of this action Industries has been advised that it has meritorious claims to support its actions for defense and indemnification.

Because of the uncertainties associated with the litigation described in (a) through (e) above, the liability of Industries and its subsidiaries alleged to be corporate successors to the former USRC cannot reasonably be estimated at this time, nor can an estimate of any ultimate liability or any insurance proceeds be made with any degree of certainty. Therefore, no such liability has been recorded in the financial statements.

(g) Blanchard Litigation

(i) Following several years of disputes and litigation involving one William C. Blanchard, a principal in an entity styled as Blanchard Securities Co. and the owner of 100 shares of Common Stock of Industries (together herein "Blanchard"), on May 22, 1986 Industries filed a lawsuit in New Jersey Superior Court, Law Division, naming Blanchard as a defendant. The action sought judicial declaration as to the status of a lease covering a small office premises in Morristown, New Jersey owned by Blanchard and subject to a long term lease entered into by Blanchard in 1955 (the "1955 Lease").

USR INDUSTRIES, INC.

Notes to Consolidated Financial Statements (Continued)

The 1955 Lease was one of several long term "credit leases" entered by Blanchard in order to utilize the credit of long term tenants to obtain construction financing for itself. As such the 1955 Lease provides for an initial term of 20 years through 1975 with four optional renewals of ten years each through 2015. After repeated demands by Industries' counsel, during 1980 Blanchard consented in writing to the sublease of the subject premises and, after further demands, during 1982 Blanchard consented to assignment of the 1955 Lease to Lighting.

In connection with the sale of the business and net assets of Lighting effective February 13, 1985 it was anticipated that the 1955 Lease would be assigned to the Purchasing Corporation. However, when Blanchard's consent to that assignment was requested, Blanchard claimed the 1955 Lease had been violated by an "unauthorized assignment" allegedly completed without Blanchard's approval and advised that Blanchard considered the 1955 Lease "terminated" and that Blanchard considered itself entitled to reenter and assume control over the premises.

In answering the litigation filed against it in Superior Court, Blanchard denied Industries' claims and interposed counterclaims alleging, inter alia, that an unauthorized assignment of the 1955 Lease had occurred and that such assignment was fraudulent, in violation of Blanchard's rights as a shareholder of Industries, in violation of fiduciary duties, securities laws, the Racketeer Influenced and Corrupt Organization Act and other related claims. Industries denied Blanchard's claims and thereupon filed a motion for summary judgment against Blanchard on one count.

On December 19, 1986 the Superior Court granted Industries' motion for summary judgment. In granting summary relief to Industries the Court held that the 1955 Lease had not been assigned as a matter of law, and remained in effect.

Blanchard took an appeal from the Superior Court decision. During late 1987 the Appellate Division affirmed the action of the Superior Court in granting summary judgment in favor of Industries. The opinion of the Appellate Division was unanimous.

Blanchard then petitioned the Supreme Court of the State of New Jersey seeking review by the Supreme Court of the unanimous Appellate Division ruling against Blanchard. By order dated March 10, 1988 the Supreme Court denied Blanchard's petition.

(ii) In a separate action begun by Blanchard in U.S. District Court for the District of New Jersey, Blanchard repeated the claims asserted in the Superior Court action discussed above, alleging fraud, breach of fiduciary duties, violations of the Racketeer Influenced and Corrupt Organization Act, securities fraud and related claims, and named as defendants Industries, Lighting, the Purchasing Corporation and certain

USR INDUSTRIES, INC.

Notes to Consolidated Financial Statements (Continued)

directors of Industries. Industries and other defendants in this action have moved to dismiss Blanchard's claims but the action has been stayed pending the outcome of the litigation begun in New Jersey Superior Court.

Industries believes that the Federal Court will give preclusive effect to the State Court judgments and that the likelihood of any material recovery against the defendants is remote.

(11) ACQUISITION OF CERTAIN REALTY ASSETS

On November 20, 1987 Industries acquired a majority interest in a commercial office building located at 550 Post Oak Boulevard, Houston, Texas 77027. The purchase was made through a Texas limited partnership, Houston-Phoenix Co., Ltd. (the "Partnership"). A wholly owned subsidiary of Industries, 550 POB, Inc. (the "Subsidiary") serves as the general partner of the Partnership and manages the property.

The building has a total of approximately 53,700 rental square feet and is approximately 75% leased, including leases with Industries, Pinnacle and Regal Petroleum, Ltd. ("Regal"), a majority owned subsidiary of Pinnacle, which will locate their offices in the building. Industries has entered into a three-year lease for approximately 2,000 rentable square feet at an initial annual rental rate of approximately \$10.00 per square foot through December 31, 1990, and Pinnacle and Regal have each entered leases having similar terms and rentals and covering approximately 1,500 rentable square feet.

To obtain the necessary financing to make the purchase Industries requested additional participation from an unaffiliated person and an officer and director of Industries, who put up the necessary additional financing through the purchase of limited partnership interests. The Partnership acquired the building from an unaffiliated third party for a total purchase price of approximately \$2,937,512. The purchase was financed through capital contributions to the Partnership totaling \$900,000 of which \$500,000 was contributed by the Subsidiary and \$400,000 through the sale of the limited partnership interests. Such interests were purchased for the same pro rata price as was paid by Industries. In addition, the limited partners made loans to the Partnership in total amount of \$100,000 and the Partnership assumed a mortgage on the property in principal amount of approximately \$1,950,000. The loans from the limited partners bear interest at 8% per annum, with the Partnership obligated to pay interest only until maturity at the earlier of December 31, 1997 or the sale of all or substantially all of the Partnership's assets. The limited partners can not be required to make any additional capital contributions to the Partnership.

In connection with the purchase transaction, the Board of Directors of Industries received the written opinion of an independent mortgage banking firm which services in excess of \$1 billion of mortgages in the Houston area to the effect that the lease terms negotiated by the Partnership with

USR INDUSTRIES, INC.

Notes to Consolidated Financial Statements (Continued)

affiliated tenants, including Industries and Pinnacle, are fair and fall within prevailing market rates for the Houston area.

The Subsidiary and the limited partners will participate in Partnership profits and distributions in proportion to their relative net capital contributions. The interest of the limited partners in the Partnership, other than any limited partnership interest which may later be acquired by the Subsidiary or the Partnership, is represented by Class A Units. For tax purposes, any Partnership losses or tax credits will be allocated one percent to the Subsidiary and ninety-nine percent to the limited partners. In addition to its participation in profits, losses and distributions of the Partnership, the Subsidiary manages the property for which the Subsidiary will be paid a management fee comparable to that generally charged for similar services in the Houston area, in no event to exceed five percent of gross revenues. In addition, the Subsidiary is reimbursed for all direct expenses incurred on behalf of the Partnership and for its general and administrative expenses allocable to Partnership operations.

Under the limited partnership agreement the Partnership, has agreed to indemnify the Subsidiary and the limited partners against certain liabilities relating to the Partnership. The partnership agreement also grants the limited partners holding Class A Units certain rights and remedies in "event of default" by the Partnership, the Subsidiary or Industries, including the right to purchase the assets of the Partnership or the Subsidiary's interest in the Partnership for fair market value, based upon an independent MAI appraisal, or to dissolve the Partnership. Under the limited partnership agreement of the Partnership an event of default includes a withdrawal of the Subsidiary as general partner, a bankruptcy, assignment for the benefit of creditors, receivership or dissolution of the Subsidiary or Industries, or breach of certain financial covenants by the Subsidiary or Industries. Upon an event of default, the Subsidiary's interest in the Partnership will be converted automatically to that of a limited partner. Any limited partnership interest held by the Subsidiary, upon conversion of the Subsidiary to a limited partner in the event of default or otherwise, will be represented by Class B Units. The voting rights of the Class B Units are generally one-tenth of those of the Class A Units. The Subsidiary has also pledged its interest in the Partnership as collateral for payment of the loans from the limited partners to the Partnership, as well as performance of the Partnership's and the Subsidiary's obligations under the partnership agreement.

As Industries, through the Subsidiary, owns a majority interest in the office building, Industries' consolidated financial statements include the assets, liabilities and the operating results of the building since the date of acquisition.

The unaudited pro forma consolidated results of operations which

USR INDUSTRIES, INC.

Notes to Consolidated Financial Statements (Continued)

follow assume that the acquisition had occurred as of January 1 in each of the periods presented.

	(in thousands, except per share amounts)	
	1987	1986
Revenues	\$ 886	1,060
Net earnings	\$ (847)	(718)
Earnings per share	\$ (.85)	(.71)

The pro forma financial information is not necessarily indicative either of results of operations that would have occurred had the purchase been made at the beginning of the period or of future results of operations of Industries, the Partnership or the presentation of the combined results hereof.

(12) INFORMATION ON SEGMENTS OF BUSINESS

Industries' significant business segments are presented below:

Real Estate. Industries' wholly owned subsidiary, 550 POB, Inc., is general partner and has a 55.6% interest in a limited partnership which during November 1987 purchased an office building. The building has total office space of approximately 53,700 net rentable square feet and is approximately 75% leased currently.

Manufacturing. Industries' manufacturing subsidiary, Metals, fabricates custom specialty dials. These dials are used as components for watches, clocks and timers for consumer and automotive applications.

Equity Ownership. Industries has an ownership interest in Pinnacle which is accounted for under the equity method of accounting. At December 31, 1987, Industries' ownership position in Pinnacle Common Stock represented approximately 44% of the total number of shares of Pinnacle Common Stock outstanding.

USR INDUSTRIES, INC.

Notes to Consolidated Financial Statements (Continued)

Year Ended December 31, 1987
(in thousands)

Sales and other income:

Real estate	\$ 44
Manufacturing	367
Other	162
	<u>\$ 573</u>

Identifiable assets:

Real estate	\$2,926
Manufacturing	347
Equity ownership	1,638
Other	923
	<u>\$5,834</u>

Earning (loss) from continuing operations:

Real Estate	\$ (39)
Manufacturing	74
Equity ownership	(544)
Other	(265)
	<u>\$ (774)</u>

Depreciation and amortization:

Real estate	\$ 10
Manufacturing	7
Other	65
	<u>\$ 82</u>

Capital expenditures:

Real estate	\$2,938
Manufacturing	4
	<u>\$2,942</u>

USR INDUSTRIES, INC.

SCHEDULE II - AMOUNTS RECEIVABLE FROM RELATED PARTIES AND UNDERWRITERS,
PROMOTERS, AND EMPLOYEES OTHER THAN RELATED PARTIES

Name of Debtor	Balance at Beginning of Period	Additions	Deductions		Balance at End of Period	
			Amounts Collected	Amounts Written Off	Current	Not Current
<u>Year ended</u> <u>December 31, 1987</u>						
AeroPanel Corporation ¹	<u>\$393,125</u>	<u>\$ 21,080</u>	<u>\$ 8,185</u>	<u>-</u>	<u>\$ 8,860</u>	<u>\$397,160</u>
MultiMetal Products Corporation ¹	<u>\$ 76,687</u>	<u>\$ 915</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>\$ 77,602</u>
<u>Year ended</u> <u>December 31, 1986</u>						
AeroPanel Corporation	<u>\$520,808</u>	<u>\$ 19,178</u>	<u>\$146,861</u>	<u>-</u>	<u>\$ 8,185</u>	<u>\$384,940</u>
MultiMetal Products Corporation	<u>\$ 75,892</u>	<u>\$ 795</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>\$ 76,687</u>
<u>Year ended</u> <u>December 31, 1985</u>						
AeroPanel Corporation	<u>-</u>	<u>\$526,099</u>	<u>\$ 5,291</u>	<u>-</u>	<u>\$116,261</u>	<u>\$404,547</u>
MultiMetal Products Corporation	<u>-</u>	<u>\$ 75,892</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>\$ 75,892</u>

¹Outstanding non-current balances due as above and current balances of \$8,860 are evidenced by notes receivable, which were discounted as of the date of their original issue to yield an assumed market interest rate of 11%. Current year additions of \$21,080 and \$915 represent amortization of discounts for fiscal 1987. Amounts collected during 1987 include the current portion of \$8,185 from 1986. Principal and interest are due in varying amounts through March 31, 1995. The notes, which are secured by all of the assets of AeroPanel Corporation and MultiMetal Products Corporation, are junior to prior secured interests of approximately \$325,000 and \$75,000, respectively.

USR INDUSTRIES, INC.

SCHEDULE VIII - VALUATION AND QUALIFYING ACCOUNTS

<u>Description</u>	<u>Balance At Beginning of Period</u>	<u>Additions Charged to Costs and Expenses</u>	<u>Deductions¹</u>	<u>Balance At End of Period</u>
<u>Year Ended December 31, 1985</u>				
Allowance for doubtful accounts	<u>\$ 26,713</u>	<u>\$ -</u>	<u>\$(26,713)</u>	<u>\$ -</u>

¹Amounts written off, net of recoveries.

USR INDUSTRIES, INC.

SCHEDULE IX - SHORT-TERM BORROWINGS

Category of aggregate short-term borrowings	Balance at end of period	Weighted average interest rate	Maximum amount outstanding during the period	Average amount outstanding during the period (A)	Weighted average interest rate during the period (B)
<u>Year ended</u> <u>December 31, 1987</u>					
Note Payable - Bank	<u>\$180,000</u>	<u>10.75%</u>	<u>\$230,000</u>	<u>\$217,500</u>	<u>11.11%</u>
<u>Year ended</u> <u>December 31, 1986</u>					
Note Payable - Bank	<u>\$230,000</u>	<u>9.50%</u>	<u>\$230,000</u>	<u>\$230,000</u>	<u>10.30%</u>
<u>Year ended</u> <u>December 31, 1985</u>					
Note Payable - Bank	<u>\$230,000</u>	<u>11.25%</u>	<u>\$530,000</u>	<u>\$344,110</u>	<u>11.65%</u>

(A) Average amount outstanding during the year is computed by dividing the total of monthly outstanding principal balances by 12.

(B) Weighted average interest rate for the year is computed by dividing the actual interest incurred from short-term borrowings by the average short-term borrowings.

USR INDUSTRIES, INC.

SCHEDULE X - SUPPLEMENTARY INCOME STATEMENT INFORMATION

<u>Item</u>	<u>Charged to</u> <u>Costs and Expenses</u>	<u>Year Ended</u> <u>December 31, 1987</u>
Taxes, other than payroll and income taxes:		
Property	\$ 5,918	

REPORT OF INDEPENDENT CERTIFIED PUBLIC ACCOUNTANTS

To the Board of Directors and
Stockholders of Pinnacle Petroleum, Inc.:

We have examined the consolidated financial statements and the financial statement schedules of Pinnacle Petroleum, Inc. and subsidiaries as listed in the index on page 15 of this Form 10-K. Our examinations were made in accordance with generally accepted auditing standards and, accordingly, included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, the financial statements referred to above present fairly the consolidated financial position of Pinnacle Petroleum, Inc. and subsidiaries as of December 31, 1987 and 1986 and the consolidated results of their operations and the changes in their financial position for each of the three years in the period ended December 31, 1987, in conformity with generally accepted accounting principles applied on a consistent basis. In addition, the financial statement schedules referred to above, when considered in relation to the basic financial statements taken as a whole, present fairly the information required to be included therein.

COOPERS & LYBRAND

Houston, Texas
March 25, 1988

PINNACLE PETROLEUM, INC.
Consolidated Balance Sheets

	December 31, 1987	December 31, 1986
<u>ASSETS</u>		
Current assets:		
Cash and short term items	\$ 2,906,406	4,134,472
Accounts receivable:		
Oil and gas sales	185,312	108,723
Drilling and operations	221,022	214,218
Other	57,505	42,833
Less allowance for doubtful accounts	(48,300)	(43,300)
Note receivable-stockholder	125,000	-
Prepaid expenses and other	66,196	37,331
Total current assets	<u>3,513,141</u>	<u>4,494,277</u>
Property and equipment, at cost:		
Oil and gas properties (using the successful efforts method of accounting)		
Producing properties	4,211,437	3,717,200
Non-producing properties	135,925	175,576
Total oil and gas properties	<u>4,347,362</u>	<u>3,892,776</u>
Pipeline	98,345	98,345
Furniture, fixtures and equipment	378,136	346,031
	<u>4,823,843</u>	<u>4,337,152</u>
Less accumulated depreciation, depletion, amortization and impairment reserve	<u>(2,469,327)</u>	<u>(1,943,006)</u>
Net property and equipment	<u>2,354,516</u>	<u>2,394,146</u>
Cost in excess of net assets acquired, net	<u>78,820</u>	<u>-</u>
	<u>\$ 5,946,477</u>	<u>6,888,423</u>

(Continued)

PINNACLE PETROLEUM, INC.

Consolidated Balance Sheets (Continued)

	December 31, 1987	December 31, 1986
<u>LIABILITIES AND STOCKHOLDERS' EQUITY</u>		
Current liabilities:		
Accounts payable:		
Trade	\$ 382,905	355,031
Production	224,768	108,333
Accrued expenses	89,445	109,630
Total current liabilities	<u>697,118</u>	<u>572,994</u>
Minority interest - Regal Petroleum, Ltd.	1,357,049	1,560,999
Series A 7.5% redeemable, cumulative, convertible preferred stock, par value \$.01; authorized, issued and outstanding 337,500 shares in 1986, stated at \$1.33 liquidation preference	-	450,000
Stockholders' equity:		
Preferred stock, par value \$.01; authorized 9,662,500 shares, none issued	-	-
Common stock, par value \$.01; authorized 15,000,000 shares, issued and outstanding 2,125,596 shares in 1987 and 1,811,958 shares in 1986	21,256	18,120
Class B convertible common stock, par value \$.01; authorized 3,500,000 shares, issued and outstanding 274,628 shares in 1987 and 1986	2,746	2,746
Additional paid-in capital	9,118,301	8,747,596
Accumulated deficit	<u>(5,249,993)</u>	<u>(4,464,032)</u>
Total stockholders' equity	<u>3,892,310</u>	<u>4,304,430</u>
	<u>\$ 5,946,477</u>	<u>6,888,423</u>

See Notes to Consolidated Financial Statements.

PINNACLE PETROLEUM, INC.

Consolidated Statements of Operations

	Years Ended		
	December 31, 1987	December 31, 1986	December 31, 1985
Revenues:			
Oil and gas production	\$ 720,123	609,811	164,007
Interest income	254,630	335,880	506,644
Gain on sale of property and equipment	9,340	66,690	-
Other	45,015	21,710	1,667
Total revenues	<u>1,029,108</u>	<u>1,034,091</u>	<u>672,318</u>
Costs and expenses:			
Production costs	482,362	473,736	50,772
Depreciation, depletion and amortization	573,918	900,766	119,349
Writedown of producing properties	-	703,000	-
Impairment reserve on non- producing properties	80,292	88,977	12,000
General and administrative	842,222	1,579,621	821,284
Amortization of cost in excess of net assets acquired	19,705	-	-
Inventory valuation reserve	-	47,974	-
Dry hole costs and abandonments	20,520	264,290	-
Total costs and expenses	<u>2,019,019</u>	<u>4,058,364</u>	<u>1,003,405</u>
Earnings (loss) from operations	(989,911)	(3,024,273)	(331,087)
Minority interest in net loss of Regal Petroleum, Ltd.	203,950	923,560	-
Equity in net loss of Regal Petroleum, Ltd.	-	-	(16,166)
Net earnings (loss)	<u>\$ (785,961)</u>	<u>(2,100,713)</u>	<u>(347,253)</u>
Net earnings (loss) per common share (after preferred dividends of \$20,000 in 1987, \$63,187 in 1986 and \$67,500 in 1985)	<u>\$ (.35)</u>	<u>(1.12)</u>	<u>(.23)</u>
Weighted average number of common shares outstanding	<u>2,333,222</u>	<u>1,937,615</u>	<u>1,785,143</u>

See Notes to Consolidated Financial Statements.

PINNACLE PETROLEUM, INC.

Consolidated Statements of Stockholders' Equity

	COMMON STOCK		CLASS B COMMON STOCK		ADDITIONAL PAID-IN	ACCUMULATED	TOTAL
	SHARES	AMOUNT	SHARES	AMOUNT	CAPITAL	DEFICIT	STOCKHOLDERS' EQUITY
Balance at December 31, 1984	1,841,908	\$18,419	-	\$ -	\$8,137,640	\$(2,016,066)	\$6,139,993
Net earnings (loss)	-	-	-	-	-	(347,253)	(347,253)
Acquisition of treasury stock (par value method)	(111,241)	(1,112)	-	-	(299,148)	-	(300,260)
Common stock issued in purchase of Spur Petroleum, Inc.	176,415	1,764	-	-	571,586	-	573,350
Dividend on redeemable preferred stock (\$.10 per share)	-	-	-	-	(67,500)	-	(67,500)
Balance at December 31, 1985	1,907,082	19,071	-	-	8,342,578	(2,363,319)	5,998,330
Net earnings (loss)	-	-	-	-	-	(2,100,713)	(2,100,713)
Class B common stock issued	(116,178)	(1,162)	274,628	2,746	448,416	-	450,000
Common stock issued to Directors for Directors' fees	27,208	272	-	-	39,728	-	40,000
Acquisition of treasury stock (par value method)	(6,154)	(61)	-	-	(19,939)	-	(20,000)
Dividend on redeemable preferred stock (\$.10 per share)	-	-	-	-	(63,187)	-	(63,187)
Balance at December 31, 1986	1,811,958	18,120	274,628	2,746	8,747,596	(4,464,032)	4,304,430
Net earnings (loss)						(785,961)	(785,961)
Common stock issued in purchase of Pinnacle Operating Company	100,000	1,000	-	-	124,000	-	125,000

(Continued)

PINNACLE PETROLEUM, INC.

Consolidated Statements of Stockholders' Equity (continued)

	COMMON STOCK		CLASS B COMMON STOCK		ADDITIONAL PAID-IN CAPITAL	ACCUMULATED DEFICIT	TOTAL STOCKHOLDERS' EQUITY
	SHARES	AMOUNT	SHARES	AMOUNT			
Common stock issued in purchase of producing properties	207,552	\$ 2,075	-	\$ -	\$ 257,365	\$ -	\$ 259,440
Common stock issued to Directors for Directors' fees	13,565	136	-	-	18,614	-	18,750
Acquisition of treasury stock (par value method)	(7,479)	(75)	-	-	(9,274)	-	(9,349)
Dividend on redeemable preferred stock (\$.10 per share)	-	-	-	-	(20,000)	-	(20,000)
Balance at December 31, 1987	<u>2,125,596</u>	<u>\$21,256</u>	<u>274,628</u>	<u>\$2,746</u>	<u>\$9,118,301</u>	<u>\$ (5,249,993)</u>	<u>\$3,892,310</u>

See Notes to Consolidated Financial Statements.

PINNACLE PETROLEUM, INC.

Consolidated Statements of Changes in Financial Position

	Years Ended		
	December 31, 1987	December 31, 1986	December 31, 1985
SOURCES OF FUNDS:			
Operations:			
Net earnings (loss)	\$ (785,961)	(2,100,713)	(347,253)
Items not affecting working capital:			
Depletion, depreciation and amortization	573,918	900,766	119,349
Writedown of producing properties	-	703,000	-
Impairment reserve on non-producing properties	80,292	88,977	12,000
Dry hole costs and abandonments	20,520	264,290	-
Amortization of cost in excess of net assets acquired	19,705	-	-
Equity in net loss of Regal Petroleum, Ltd.	-	-	16,166
Minority interest in net loss of Regal Petroleum, Ltd.	(203,950)	(923,560)	-
(Gain) loss on sale of property and equipment	(9,340)	(66,690)	-
Funds provided by (used for) operations	(304,816)	(1,133,930)	(199,738)
Proceeds from sale of property and equipment	20,248	145,926	265
Issuance of and conversion to Class B common stock	-	450,000	-
Common stock issued to directors	18,750	40,000	-
Decrease in other assets	-	541	872
Decrease in working capital	1,105,260	1,339,778	663,474
	<u>\$ 839,442</u>	<u>842,315</u>	<u>464,873</u>

(Continued)

PINNACLE PETROLEUM, INC.

Consolidated Statements of Changes in Financial Position (Continued)

	Years Ended		
	December 31, 1987	December 31, 1986	December 31, 1985
USES OF FUNDS:			
Additions of oil and gas properties \$	346,186	172,730	13,270
Treasury stock acquisitions	9,349	20,000	300,260
Decrease in minority interest in net assets of Regal Petroleum, Ltd.	-	27,700	-
Conversion and redemption of redeemable preferred stock	450,000	450,000	-
Decrease in ownership of investee prior to consolidation	-	-	16,166
Additions of other property and equipment	39,482	108,698	148,134
Dividends on redeemable preferred stock	20,000	63,187	67,500
Assets and liabilities acquired, net of working capital:			
Oil and gas properties	259,440	-	3,782,672
Property and equipment	900	-	122,480
Cost in excess of net assets acquired	98,525	-	-
Issuance of common stock for net assets of subsidiaries	(198,211)	-	(573,350)
Issuance of common stock for oil and gas properties	(186,229)	-	-
Issuance of redeemable preferred stock	-	-	(900,000)
Minority interest in net assets of Regal Petroleum, Ltd.	-	-	(2,512,259)
	<u>\$ 839,442</u>	<u>842,315</u>	<u>464,873</u>

(Continued)

PINNACLE PETROLEUM, INC.

Consolidated Statements of Changes in Financial Position (Continued)

	Years Ended		
	December 31, 1987	December 31, 1986	December 31, 1985
CHANGES IN COMPONENTS OF WORKING CAPITAL:			
Increase (decrease) in current assets:			
Cash and short term items	\$ (1,228,066)	(1,123,539)	(592,548)
Accounts receivable, net	93,065	(255,007)	401,453
Note receivable-stockholder	125,000	-	-
Prepaid expenses and other	28,865	(64,267)	101,598
	<u>(981,136)</u>	<u>(1,442,813)</u>	<u>(89,497)</u>
Increase (decrease) in current liabilities:			
Accounts payable	144,309	(114,409)	495,721
Accrued expenses	(20,185)	11,374	78,256
	<u>124,124</u>	<u>(103,035)</u>	<u>573,977</u>
Increase (decrease) in working capital	<u>\$ (1,105,260)</u>	<u>(1,339,778)</u>	<u>(663,474)</u>

See Notes to Consolidated Financial Statements

PINNACLE PETROLEUM, INC.

Notes to Consolidated Financial Statements

(1) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Principles of Consolidation

The consolidated financial statements include the accounts of Pinnacle Petroleum, Inc. (the "Company"), its wholly owned subsidiaries, PinReg Corporation ("PinReg"), Spur Petroleum, Inc. ("Spur"), Pinnacle Operating Company, Woodstead Petroleum Corporation and PinReg's majority owned subsidiary, Regal Petroleum, Ltd. ("Regal"). All significant intercompany accounts and transactions have been eliminated in consolidation.

Oil and Gas Properties

The Company follows the successful efforts method of accounting for its oil and gas properties. Under the successful efforts method, costs associated with the acquisition, drilling and equipping of successful exploratory wells and all developmental costs are capitalized and amortized using the unit-of-production method. Geological and geophysical costs, delay rentals and drilling costs of unsuccessful exploratory wells are charged to expense as incurred. The Company also recognized a writedown of producing properties of \$703,000 in 1986. The writedown was the result of comparing the estimated undiscounted cash flows of the Company's reserves using year end gas prices and assuming an oil price of \$17.50 per barrel to the carrying value of the producing properties.

Proceeds from the sale of an interest in a non-producing oil and gas property are credited to the asset account until all capitalized costs are recovered relative to that property. Any proceeds received in excess of cost are recorded as a gain.

The Company reevaluates the carrying value of its non-producing properties from time to time in light of economic circumstances and provides an impairment reserve which is charged to operations in the year in which such determination is made.

Property and Equipment

Property and equipment are being depreciated over their estimated useful lives using the straight line method. Expenditures for maintenance and repairs which do not improve or extend the useful lives are charged to operations as incurred, while expenditures for major renewals and betterments are capitalized. Dispositions of assets are reflected at the historical costs less accumulated depreciation, with the resulting gain or loss reflected in operations currently.

PINNACLE PETROLEUM, INC.

Notes to Consolidated Financial Statements (Continued)

Earnings Per Share

Earnings per share of Common Stock and common equivalent share are computed by dividing net earnings after preferred stock dividend requirements by the weighted average number of shares of Common Stock outstanding during each period. Conversion of preferred stock and exercise of options and Warrants to acquire shares of common stock are included in the computation of earnings per share of Common Stock to the extent that they are dilutive. Fully diluted earnings per share are not presented because such data would not be significantly different from the amounts shown.

Financial Accounting Standards Board's ("FASB") Statement Release

The FASB issued Statement of Financial Accounting Standards ("SFAS") No. 96 "Accounting for Income Taxes" in December 1987. The SFAS requires substantial changes in the method of accounting for deferred income taxes and must be adopted by the Company beginning in 1989. The Company has no deferred taxes recorded and is currently in a net operating loss carryforward position. The Company has not yet adopted SFAS No. 96 and accordingly, the impact on the Company's financial condition and results of operations has not been determined; however, the Company does not expect it to have a material adverse effect.

Income Taxes

The Company and its wholly owned subsidiaries join in filing a consolidated federal income tax return. Investment tax credits are accounted for by the flow-through method.

Reclassifications

Certain amounts from prior periods have been reclassified to conform to the presentation format for the consolidated financial statements as of December 31, 1987 with no effect on reported results of operations.

(2) OIL AND GAS PRODUCING ACTIVITIES

The Company's oil and gas operations are conducted entirely in the United States. Aggregate capitalized costs relating to these operations and related accumulated depletion, depreciation and amortization are as follows:

CAPITALIZED COSTS

	Years Ended December 31,		
	1987	1986	1985
Oil and Gas Properties:			
Proved	\$ 4,211,437	3,717,200	3,688,911
Unproved	135,925	175,576	813,886
	<u>4,347,362</u>	<u>3,892,776</u>	<u>4,502,797</u>
Less accumulated depreciation, depletion and amortization	<u>(2,285,041)</u>	<u>(1,835,980)</u>	<u>(696,369)</u>
Net oil and gas properties	<u>\$ 2,062,321</u>	<u>2,056,796</u>	<u>3,806,428</u>

PINNACLE PETROLEUM, INC.

Notes to Consolidated Financial Statements (Continued)

Costs incurred in the Company's oil and gas operations and related accumulated depreciation, depletion and amortization per equivalent unit-of-production are as follows:

	Years Ended December 31,		
	1987	1986	1985
Property acquisition costs:			
Proved	\$ 511,694	2,251	-
Unproved	4,341	964	13,270
	<u>\$ 516,035</u>	<u>3,215</u>	<u>13,270</u>
Exploration costs	<u>\$ 78,976</u>	<u>210,992</u>	<u>7,828</u>
Development costs	<u>\$ 65,443</u>	<u>-</u>	<u>-</u>
Depletion and depreciation	<u>\$ 488,381</u>	<u>1,524,346⁽¹⁾</u>	<u>96,168</u>
Depletion and depreciation per equivalent unit of production	<u>\$ 9.87</u>	<u>35.73</u>	<u>15.28</u>

(1) Includes writedown of producing properties of \$703,000.

SALES AND REVENUES FROM OIL AND GAS PRODUCING ACTIVITIES

The Company sells its oil and gas production on currently available markets and pursuant to contracts with various purchasers. For the year ended December 31, 1987 sales to two purchasers accounted for approximately 21% and 13% of total revenues. For the year ended December 31, 1986 sales to three purchasers accounted for approximately 12%, 12% and 10% of total revenues. Management believes that if such purchasers were not available, the Company would be able to sell its production to other purchasers on equivalent terms and conditions.

(3) PURCHASE OF COMMON STOCK OF REGAL PETROLEUM, LTD. AND SPUR PETROLEUM, INC.

During 1985 a wholly owned subsidiary of the Company acquired Common Stock in Regal Petroleum, Ltd. and as of December 31, 1985 owned slightly in excess of 50% of the shares of Regal Common Stock outstanding. The transaction was accounted for using the purchase method of accounting. The subsidiary purchased the Common Stock in open market and private transactions as well as through a direct private placement consideration of \$3,190,987. For the fiscal year ended December 31, 1985 the pro rata equity share of operating earnings of Regal was included in the Statement of Operations under the caption "Equity in net earnings (loss) of Regal Petroleum, Ltd." For 1986 and 1987 the accounts of Regal are fully consolidated with those of Pinnacle and its wholly owned subsidiaries.

PINNACLE PETROLEUM, INC.

Notes to Consolidated Financial Statements (Continued)

Pursuant to an agreement dated November 27, 1985 between a wholly owned subsidiary of the Company, and Spur Petroleum, Inc., a privately held Texas company based in Amarillo, Texas, the Company agreed to acquire by merger all of the outstanding Common Stock of Spur. In the transaction, Spur stockholders received 176,415 unregistered shares of Common Stock of the Company.

(4) PURCHASE OF CERTAIN PROPERTIES

During 1987 through a wholly owned subsidiary the Company purchased certain oil and gas working interests from five unaffiliated partnerships. The subject working interests acquired are located in Oklahoma, Kansas, Wyoming and New York. The partnerships received as consideration in exchange for the working interests conveyed an aggregate of 148,983 unregistered shares of Pinnacle Common Stock. The Company recorded the properties at \$186,229.

The unaudited pro forma consolidated results of operations which follow assume that the acquisition had occurred as of January 1, 1986. The 1987 pro forma information is not presented as the acquisition was effective January 1, 1987.

(in thousands except per share amounts)

	<u>1986</u>
Revenues	\$ 1,027
Net earnings	\$(2,042)
Earnings per share	\$ (1.01)

The pro forma financial information is not necessarily indicative either of results of operations that would have occurred had the purchase been made at the beginning of the period or of future results of operations of the Company or the presentation of consolidated results hereof.

Additionally, the Company acquired V-Mc Operating Company, an operator of 24 oil and gas wells, through a wholly owned subsidiary for 100,000 unregistered shares of Common Stock. The Company recorded the acquisition at \$125,000. The acquisition has been recorded as a purchase with the purchase price allocated to the fair value of the net assets acquired. The cost in excess of net assets acquired of \$98,525 is being amortized over five years. The Company also acquired interests in oil and gas properties, through a wholly owned subsidiary, for 58,569 unregistered shares of Common Stock. The acquisition was recorded at \$73,211. No pro forma information is presented on the above acquisitions since their effects are not material.

PINNACLE PETROLEUM, INC.

Notes to Consolidated Financial Statements (Continued)

(5) COMMON STOCK

An Employees' Stock Option Plan covering 184,000 shares of Common Stock was approved by stockholders at the Annual Meeting held July 31, 1984. On July 30, 1986 the Board of Directors granted options to two officers of the Company exercisable at prices per share of \$1.49 and \$1.35, respectively. One officer's option for 150,000 shares is exercisable in whole or in part through July 30, 1991. The other officer's option for 30,000 shares is exercisable in whole or in part through July 30, 1996. No other rights or options have been granted under the Option Plan and no options were exercised during 1987 or 1986.

At the Annual Meeting held November 14, 1986 stockholders approved the issuance a new class of common stock designated Class B Common Stock ("Class B Common"). The holders of Class B Common, voting as a separate class, have the right to elect a simple majority of the Board of Directors and vote as a separate class on major corporate transactions. Holders of the Class B Common vote share-for-share with holders of the Common Stock and Series A Preferred Stock on all other matters. Holders of Common Stock, but not of Class B Common, received a Warrant Dividend exercisable at various prices during two future exercise periods. (See Note 7) While the Class B Common is not entitled to such Warrant Dividend but otherwise participates equally share-for-share with the Common Stock in dividends and distributions.

The Common Stock is admitted for listing on NASDAQ and continues to be publicly tradeable. Class B Common shares are not publicly tradeable, and are only transferable to persons within defined categories of "permitted transferees," but may be converted into Common Stock at any time on a share-for-share basis.

(6) REDEEMABLE PREFERRED STOCK

On June 28, 1985 the Company issued to Titan Wells, Inc. ("Titan") whose principal stockholder is the Company's Chairman, 675,000 shares of Series A Convertible Voting Preferred Stock ("Series A Preferred Stock"), par value \$.01 per share, together with warrants (see Note 7 "Warrants") to purchase up to 200,000 shares of its Common Stock through December 1990. In consideration of the issuance of such Series A Preferred Stock and the warrants, the Company received from Titan \$450,000 cash; working interests in various proved producing oil and gas properties and certain undeveloped leases in Michigan. Each share of Series A Preferred Stock is entitled to one vote per share and votes with the common stock of the Company as a single class. Each share of Series A Preferred Stock is convertible into .4444 shares of Common Stock based on the current conversion price of \$3.00 per share.

The Series A Preferred Stock required a sinking fund be established for the redemption of the stock with annual sums sufficient to redeem twenty percent of the shares then outstanding beginning on June 30 of each of the years 1991 through 1995 at a price of \$1.33 per share plus accrued, unpaid dividends, whether or not declared. Should the Company be unable to redeem such shares, the preferred stockholders shall be entitled to elect two additional directors of the Company.

PINNACLE PETROLEUM, INC.

Notes to Consolidated Financial Statements (Continued)

Titan exchanged 337,500 shares of Series A Preferred Stock under the terms of the Class B Common exchange offer on November 20, 1986 and received 158,450 shares of Class B. During 1987, the Company redeemed the remaining 337,500 shares of the Series A Preferred Stock for a net price of \$436,500.

(7) WARRANTS

In conjunction with the issuance to Titan of Series A Preferred Stock the Company also issued warrants to purchase up to 200,000 shares of common stock through December 1990. The warrants are exercisable from March 1, 1986 through December 31, 1990 at a price of \$3.00 per share. The exercise price of the warrants is subject to an anti-dilution adjustment. To date, no warrants have been exercised and the exercise price as of December 31, 1987 was \$2.46 per share.

The Board of Directors declared a dividend of Common Stock Purchase Warrants (the "Warrant Dividend") which entitled all stockholders of record on November 20, 1986 to receive one warrant to purchase one share of Common Stock for every five shares of Common Stock owned. The Warrants are exercisable during two 60-day periods, the first exercise period starting on April 1, 1988 (the beginning of which period has, pursuant to terms of the Warrant, been postponed for 180 days) and the second exercise period starting 12 months after the first period begins (but also subject to postponement by the Company for an additional 180 days.) The exercise price of the Warrants during the first exercise period is \$1.35 and \$1.50 during the second exercise period. There were a total of 363,082 Warrants issued to stockholders.

(8) INCOME TAXES

For federal income tax purposes, at December 31, 1987 the Company had net operating loss carryforwards of approximately \$4,989,000 which expire at various dates through the year 2002 and investment tax credit carryforwards of approximately \$34,700 which expire at various dates through the year 2000.

For financial reporting purposes, at December 31, 1987 the Company had \$6,908,000 of net operating loss carryforwards and approximately \$37,000 of net investment tax credit carryforwards. Certain items of income and expense, primarily depreciation, depletion and intangible drilling costs, are recognized for income tax purposes in amounts and periods which differ from those recognized for financial reporting purposes. Investment tax credit carryovers for income tax and financial reporting purposes have been reduced in accordance with the Tax Reform Act of 1986.

(9) CERTAIN TRANSACTIONS

During June 1985 the Company sold and issued to Titan 675,000 unregistered and redeemable shares of Series A Convertible Voting Preferred Stock, together with warrants to purchase up to 200,000 shares of the Company's Common Stock through December 1990 at a price of \$3.00 per share. The Company's Chairman also serves as chief executive officer and is the principal stockholder of Titan. In connection with its review of the

PINNACLE PETROLEUM, INC.

Notes to Consolidated Financial Statements (Continued)

transaction, the Board of Directors retained an independent investment banking firm, Sutro & Co. Incorporated, which delivered to the Company its written opinion that the transaction was fair, from a financial point of view, to the Company and to the holders of its Common Stock.

Allocation of certain general and administrative expenses of personnel, office equipment and facilities shared with an affiliate are subject to a Corporate Separation Agreement approved by the Board of Directors of the Company and USR Industries, Inc., the parties thereto. For the year ended December 31, 1985 such expenses allocated to the Company under such agreement was approximately \$27,000. Thereafter, as such general and administrative expenses have been fully segregated and are charged directly no expense allocation was made for the years ended December 31, 1987 and 1986.

During June 1985, the Company purchased 111,111 shares of its Common Stock from USR Industries, Inc. for a net purchase price of \$300,000, or \$2.70 per share. On the purchase date, the Company's Common Stock was reported in the over-the-counter market as \$1.50 bid and \$1.75 asked per share.

In order to conserve working capital and to provide Directors of the Company an equity stake in the future growth and development in the Company, Directors have agreed to accept shares of Common Stock of the Company in lieu of cash compensation for their services as Directors. During the years ended December 31, 1987 and 1986 each Director received \$5,000 of newly issued shares of Common Stock for their services as Director. During the year ended December 31, 1985 the Company incurred legal fees of approximately \$97,534 to a law firm in which a Director of the Company is a partner.

On December 31, 1987 the Company advanced the Chairman, who is also a stockholder, a total of \$125,000 on a short term basis, with such loan plus accrued interest at a 10% annual rate being due and payable on March 31, 1988, and renewed for 90 days to June 30, 1988. Separately, the Company's majority owned subsidiary advanced an additional \$75,000 to the Chairman on January 27, 1988 on a short term basis due June 30, 1988. Such advances were personally guaranteed in full by the Chairman and secured by the pledge, respectively, of a 22% working interest in certain producing properties and the pledge of 75,000 shares of Common Stock of the Company.

(10) SUPPLEMENTAL OIL AND GAS INFORMATION (UNAUDITED)

The following quantity and discounted estimates of future cash flows are based on prices as of the respective year ends. No price escalations were assumed except for gas sales made under terms of contracts which include fixed and determinable escalations. Operating costs, production taxes, windfall profit tax, royalties and estimated future capital expenditures to complete development of the proved reserves were deducted in determining the quantity and discounted estimates of future cash flows. Such costs were estimated based on current costs and were not adjusted to anticipate increases due to inflation or other factors. No deductions were made for general overhead, depreciation or other indirect costs.

PINNACLE PETROLEUM, INC.

Notes to Consolidated Financial Statements (Continued)

ANALYSIS OF CHANGES IN PROVED RESERVES

	Years Ended December 31,					
	1987		1986		1985	
	Oil (Bbls)	Gas (Mcf)	Oil (Bbls)	Gas (Mcf)	Oil (Bbls)	Gas (Mcf)
PROVED DEVELOPED AND UNDEVELOPED RESERVES:						
Beginning of year	101,429	592,791	193,577	926,943	8,809	3,585
Revisions of previous estimates	33,737	(38,653)	(68,257)	(228,037)	997	12,468
Extensions, discoveries and other additions	1,055	38,053	-	-	-	-
Production	(28,181)	(127,733)	(24,503)	(108,936)	(4,022)	(13,626)
Purchases of minerals in place	47,461	685,732	612	2,821	187,793	924,516
End of year	(1) 155,501	(1) 1,150,190	(2) 101,429	(2) 592,791	(3) 193,577	(3) 926,943

PROVED DEVELOPED RESERVES:

Beginning of year	94,880	589,025	180,015	915,990	8,809	3,585
End of year	(1) 148,951	(1) 968,805	(2) 94,880	(2) 589,025	(3) 180,015	(3) 915,990

- (1) Proved Reserves include 45,790 barrels and 235,622 Mcf and Proved Developed Reserves included 45,790 barrels and 192,222 Mcf of reserves attributable to the minority interest in Regal Petroleum, Ltd.
- (2) Proved and Proved Developed Reserves include 41,516 barrels and 212,346 Mcf of reserves attributable to the minority interest in Regal Petroleum, Ltd.
- (3) Proved and Proved Developed Reserves include 66,736 barrels and 352,606 Mcf of reserves attributable to the minority interest in Regal Petroleum, Ltd.

PINNACLE PETROLEUM, INC.

Notes to Consolidated Financial Statements (Continued)

STANDARDIZED MEASURE OF DISCOUNTED FUTURE NET
CASH FLOWS AND CHANGES THEREIN

The standardized measure of discounted future net cash flows and changes therein relating to proved oil and gas reserves is as follows:

	Years Ended December 31,		
	1987	1986	1985
Future cash inflows	\$ 4,786,756	2,849,096	7,443,262
Future production and development costs	(1,819,475)	(1,040,658)	(2,243,910)
Future income tax expenses	-	-	-
Future net cash flows	2,967,281	1,808,438	5,199,352
10% annual discount for estimated timing of cash flows	<u>(1,030,339)</u>	<u>(489,688)</u>	<u>(1,507,610)</u>
Standardized measure of discounted future net cash flows	<u>\$ 1,936,942⁽¹⁾</u>	<u>1,318,750⁽²⁾</u>	<u>3,691,742</u>

Future net cash flows were computed using year-end prices and costs, and year-end statutory tax rates that relate to existing proved oil and gas reserves.

- (1) Includes \$507,810 of estimated discounted future net revenues attributable to the minority interest in Regal Petroleum, Ltd.
- (2) Includes \$460,850 of estimated discounted future net revenues attributable to the minority interest in Regal Petroleum, Ltd.
- (3) Includes \$1,023,215 of estimated discounted future net revenues attributable to the minority interest in Regal Petroleum, Ltd.

PINNACLE PETROLEUM, INC.

Notes to Consolidated Financial Statements (Continued)

The following are the principal sources of change in the standardized measure of discounted future net cash flows:

	Years Ended December 31,		
	1987	1986	1985
Standardized measure of discounted future net cash flows	\$ 1,318,750	3,691,742	138,035
Sale of oil and gas produced, net of production costs	(237,761)	(183,593)	(38,320)
Net changes in prices and production costs	(238,497)	(1,441,482)	64,008
Purchase of minerals in place	729,285	9,998	3,448,165
Extensions and discoveries	53,519	-	-
Revision of previous quantity estimates	179,771	(1,127,089)	66,051
Accretion of discount	131,875	369,174	13,803
Net change in income taxes	-	-	-
Standardized measure of discounted future net cash flows	<u>\$ 1,936,942⁽¹⁾</u>	<u>1,318,750⁽²⁾</u>	<u>3,691,742⁽³⁾</u>

Future net cash flows were computed using year-end prices and costs, and year-end statutory tax rates that relate to existing proved oil and gas reserves.

(1) Includes \$507,810 of estimated discounted future net revenues attributable to the minority interest in Regal Petroleum, Ltd.

(2) Includes \$460,850 of estimated discounted future net revenues attributable to the minority interest in Regal Petroleum, Ltd.

(3) Includes \$1,023,215 of estimated discounted future net revenues attributable to the minority interest in Regal Petroleum, Ltd.

PINNACLE PETROLEUM, INC.

SCHEDULE V - PROPERTY AND EQUIPMENT

<u>Classification</u>	<u>Beginning of Period</u>	<u>Additions at Cost</u>	<u>Retirements</u>	<u>Other Changes Add (Deduct)</u>	<u>At End of Period</u>
<u>Year Ended December 31, 1985</u>					
Oil and gas properties	\$ 762,358	13,270	(55,503)	3,782,672	4,502,797
Pipeline	-	-	-	98,345	98,345
Furniture, fixtures and equipment	<u>134,591</u>	<u>148,134</u>	<u>(13,002)</u>	<u>24,135</u>	<u>293,858</u>
	<u>\$ 896,949</u>	<u>161,404</u>	<u>(68,505)</u>	<u>3,905,152¹</u>	<u>4,895,000</u>
<u>Year Ended December 31, 1986</u>					
Oil and gas properties	\$4,502,797	172,730	(782,751)	-	3,892,776
Pipeline	98,345	-	-	-	98,345
Furniture, fixtures and equipment	<u>293,858</u>	<u>108,698</u>	<u>(56,525)</u>	<u>-</u>	<u>346,031</u>
	<u>\$4,895,000</u>	<u>281,428</u>	<u>(839,276)</u>	<u>-</u>	<u>4,337,152</u>
<u>Year Ended December 31, 1987</u>					
Oil and gas properties	\$3,892,776	605,626	(151,040)	-	4,347,362
Pipeline	98,345	-	-	-	98,345
Furniture, fixtures and equipment	<u>346,031</u>	<u>40,382</u>	<u>(8,277)</u>	<u>-</u>	<u>378,136</u>
	<u>\$4,337,152</u>	<u>646,008</u>	<u>(159,317)</u>	<u>-</u>	<u>4,823,843</u>

¹Amounts reflect purchase of Spur Petroleum, Inc. and a majority interest in Regal Petroleum, Ltd.

PINNACLE PETROLEUM, INC.

SCHEDULE VI - ACCUMULATED DEPRECIATION, DEPLETION, AND
AMORTIZATION OF PROPERTY AND EQUIPMENT

<u>Classification</u>	<u>Balance at Beginning of Period</u>	<u>Additions Charged to Costs and Expenses</u>	<u>Retirements</u>	<u>Other Changes Add (Deduct)</u>	<u>Balance At End of Period</u>
<u>Year Ended December 31, 1985</u>					
Oil and gas properties	\$ 643,939	108,168	(55,738)	-	696,369
Furniture, fixtures and equipment	<u>38,965</u>	<u>23,181</u>	<u>(12,502)</u>	<u>-</u>	<u>49,644</u>
	<u>\$ 682,904</u>	<u>131,349</u>	<u>(68,240)</u>	<u>-</u>	<u>746,013</u>
<u>Year Ended December 31, 1986</u>					
Oil and gas properties	\$ 696,369	1,613,323	(473,712)	-	1,835,980
Pipeline	-	5,567	-	-	5,567
Furniture, fixtures and equipment	<u>49,644</u>	<u>73,853</u>	<u>(22,038)</u>	<u>-</u>	<u>101,459</u>
	<u>\$ 746,013</u>	<u>1,692,743</u>	<u>(495,750)</u>	<u>-</u>	<u>1,943,006</u>
<u>Year Ended December 31, 1987</u>					
Oil and gas properties	\$1,835,980	568,673	(119,612)	-	2,285,041
Pipeline	5,567	9,278	-	-	14,845
Furniture, fixtures and equipment	<u>101,459</u>	<u>76,259</u>	<u>(8,277)</u>	<u>-</u>	<u>169,441</u>
	<u>\$1,943,006</u>	<u>654,210</u>	<u>(127,889)</u>	<u>-</u>	<u>2,469,327</u>

PINNACLE PETROLEUM, INC.

SCHEDULE VIII - VALUATION AND QUALIFYING ACCOUNTS

<u>CLASSIFICATION</u>	<u>BALANCE AT BEGINNING OF PERIOD</u>	<u>ADDITIONS CHARGED TO COSTS AND EXPENSES</u>	<u>RETIREMENTS¹</u>	<u>BALANCE AT END OF PERIOD</u>
<u>Year Ended December 31, 1985</u>				
Allowance for doubtful accounts	<u>\$ 59,539</u>	<u>44,314</u>	<u>(58,192)</u>	<u>45,661</u>
<u>Year Ended December 31, 1986</u>				
Allowance for doubtful accounts	<u>\$ 45,661</u>	<u>43,300</u>	<u>(45,661)</u>	<u>43,300</u>
<u>Year Ended December 31, 1987</u>				
Allowance for doubtful accounts	<u>\$ 43,300</u>	<u>5,000</u>	<u>-</u>	<u>48,300</u>

¹Accounts written off, net of recoveries.

PINNACLE PETROLEUM, INC.

SCHEDULE X - SUPPLEMENTARY INCOME STATEMENT INFORMATION

<u>Item</u>	<u>Charged to</u> <u>Costs and Expenses</u>	
	<u>Years Ended December 31,</u> <u>1987</u>	<u>1986</u>
Taxes, other than payroll and income taxes:		
Production	\$ 17,092	\$ 20,718
Property	17,954	48,150
Franchise	<u>20,418</u>	<u>32,191</u>
	<u>\$ 55,464</u>	<u>\$101,059</u>

USR INDUSTRIES, INC.

Item 9. Disagreements on Accounting and Financial Disclosure.

None.

PART III

Item 10. Directors and Executive Officers of the Registrant.

The definitive Proxy Statement in connection with the 1988 Annual Meeting of Stockholders to be filed by the Corporation pursuant to Regulation 14A of the Securities Exchange Act of 1934 not later than 120 days after December 31, 1987 is incorporated herein by reference.

Item 11. Executive Compensation.

The definitive Proxy Statement in connection with the 1988 Annual Meeting of Stockholders to be filed by the Corporation pursuant to Regulation 14A of the Securities Exchange Act of 1934 not later than 120 days after December 31, 1987 is incorporated herein by reference.

Item 12. Security Ownership of Certain Beneficial Owners and Management.

The definitive Proxy Statement in connection with the 1988 Annual Meeting of Stockholders to be filed by the Corporation pursuant to Regulation 14A of the Securities Exchange Act of 1934 not later than 120 days after December 31, 1987 is incorporated herein by reference.

Item 13. Certain Relationships and Related Transactions.

The definitive Proxy Statement in connection with the 1988 Annual Meeting of Stockholders to be filed by the Corporation pursuant to Regulation 14A of the Securities Exchange Act of 1934 not later than 120 days after December 31, 1987 is incorporated herein by reference.

USR INDUSTRIES, INC.

PART IV

Item 14. Exhibits, Financial Statement Schedules and Reports on Form 8-K.

(a) Exhibits, Financial Statements and Financial Statement Schedules.

(1) and (2) Financial Statements and Financial Statement Schedules.

See Index to Financial Statements and Related Schedules included in Item 8 (Financial Statements and Supplementary Data).

(b) Reports on Form 8-K

Form 8-K dated November 20, 1987 relating to the acquisition of an office building.

(c) Exhibits

The following exhibits are filed as part of this report. Where such filing is made by incorporation by reference to a previously filed statement or report, such statement or report is identified in parenthesis.

3. Articles of Incorporation and Bylaws

3.1 Certificate of Incorporation (incorporated by reference to Exhibit 3(a) of Form 8-B dated October 15, 1980)

3.2 Amendment to Certificate of Incorporation filed on June 13, 1984 (incorporated by reference to Exhibit 3 of Form 10-K for year ended December 31, 1984)

3.3 Bylaws (incorporated by reference to Exhibit 3(b) of Form 8-B dated October 15, 1980)

10. Material Contracts

10.1 Stock Purchase Agreement between USR Industries, Inc. and Pinnacle Petroleum, Inc. dated July 19, 1983 and Modification Agreement thereto dated September 18, 1983 (incorporated by reference to Exhibits 10(a) and 10(b) of Form 10-K of Pinnacle Petroleum, Inc. for the year ended August 31, 1983) (File No. 0-9946)

10.2 Assets Purchase Agreement between USR Lighting, Inc. and AeroPanel Corporation (incorporated by reference to Exhibit 2(a) of Form 8-K dated March 8, 1985)

10.3 Assets Purchase Agreement between USR Metals, Inc. and MultiMetal Products Corporation (incorporated by reference to Exhibit 2(b) of Form 8-K dated March 8, 1985)

10.4 Lease dated as of December 12, 1983 between USR Lighting, Inc. and 661 Myrtle Property Co., Ltd. (incorporated by reference to Exhibit 10 of Form 10-K for year ended December 31, 1984)

10.5 Employee's Incentive Stock Option Plan (incorporated by reference to Exhibit 10 of Form 10-K for year ended December 31, 1984)

22. Subsidiaries of USR Industries, Inc.

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the Company and in the capacities and on the dates indicated.

Date: March 29, 1988

By: /s/ Ralph T. McElvenny, Jr.

Ralph T. McElvenny, Jr.
Chairman of the Board
(Principal Executive and
Financial Officer)

Date: March 29, 1988

By: /s/ Anthony N. Cialone

Anthony N. Cialone, Director

Date: March 29, 1988

By: /s/ Stephen C. Miller

Stephen C. Miller
Treasurer
(Principal Accounting Officer)

Date: March 29, 1988

By: /s/ Charles R. White

Charles R. White, Director

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the Company and in the capacities and on the dates indicated.

Date: March 29, 1988

By:

Ralph T. McElvenny, Jr.
Chairman of the Board
(Principal Executive and
Financial Officer)

Date: March 29, 1988

By:

Anthony N. Cialone, Director

Date: March 29, 1988

By:

Stephen C. Miller
Treasurer
(Principal Accounting Officer)

Date: March 29, 1988

By:

Charles R. White, Director

(8)

400,000 Shares
Pinnacle Petroleum, Inc.
Common Stock
(\$0.01 Par Value)
\$1.15 Per Share

All of the 400,000 shares of Common Stock of Pinnacle Petroleum, Inc. ("Pinnacle" or the "Company") offered hereby (the "Shares") are being offered by USR Industries, Inc. ("Industries") to Industries' stockholders of record on July 20, 1988 (the "Industries Stockholders"). The Shares are being offered at a price of \$1.15 per Share. Industries will receive all of the proceeds from the sale of Shares offered hereby. Pinnacle will not receive any of such proceeds.

The Shares of Pinnacle Common Stock being offered have voting and other rights customary for common stock, subject to the rights of Pinnacle's Class B Common Stock. As previously approved by Pinnacle's stockholders at a stockholders' meeting held on November 14, 1986, the Class B Common Stock is entitled to vote as a separate class to elect a majority of the Company's Board of Directors and to vote on major corporate transactions. Pinnacle Common Stock is entitled to vote on a share-for-share basis with the Company's Class B Common Stock as to the election of a minority of the Board of Directors. For a more complete description of the rights of the holders of Pinnacle Common Stock and of the Class B Common Stock, see "Description of Pinnacle Common Stock."

Each Industries Stockholder who has subscribed for the maximum number of Shares initially made available to him will have the opportunity to subscribe, at the same price, for a pro rata portion of any Shares which are not subscribed for by other Industries Stockholders. Thereafter, if any Shares remain unsold, any participant, to any extent, in this offering may purchase such remaining Shares on a pro rata basis in the event such Shares are offered by Industries (See "How to Subscribe").

Certain members of Industries' and Pinnacle's management who are also Industries Stockholders, including Ralph T. McElvenny, Jr., who serves as Chief Executive Officer of Industries and of Pinnacle, have indicated that they intend to purchase all Shares to which they are entitled in the initial offer and Mr. McElvenny has indicated that he intends to purchase all of the Shares to which he is entitled in the offer of Shares not subscribed for in the initial offering. For information concerning Industries and the plan of distribution of the Shares, see "Information About Selling Stockholder" and "The Offering."

Pinnacle Common Stock is traded in the over-the-counter market under the symbol PNCL. The average of the closing bid and asked prices for the three months preceding this offering as reported by the National Association of Securities Dealers Automated Quotation System, were \$1.12 and \$1.36, respectively. For factors that were considered in determining the Subscription Price, see "The Offering."

**THIS OFFERING WILL EXPIRE AT 3:00 P.M., MOUNTAIN TIME, ON AUGUST 31, 1988,
UNLESS EXTENDED BY INDUSTRIES, IN ITS DISCRETION.**

**THE SECURITIES OFFERED HEREBY INVOLVE A HIGH DEGREE OF RISK.
SEE "RISK FACTORS."**

**THESE SECURITIES HAVE NOT BEEN APPROVED OR DISAPPROVED BY THE
SECURITIES AND EXCHANGE COMMISSION NOR HAS THE COMMISSION
PASSED UPON THE ACCURACY OR ADEQUACY OF THIS PROSPECTUS.
ANY REPRESENTATION TO THE CONTRARY IS A CRIMINAL OFFENSE.**

The total price to the Industries Stockholders, if all of the Shares are acquired, would be \$460,000. All of the price paid by the purchasers of the Shares offered herein, after deducting expenses, including registration and filing fees, legal fees, subscription and other fees, which are estimated to total \$40,000, will be received by Industries. No underwriting discounts or commissions will be paid in connection with the sale of the Shares offered hereby.

The date of this Prospectus is August 3, 1988.

XXIX-008

AVAILABLE INFORMATION

Pinnacle is subject to the informational requirements of the Securities Exchange Act of 1934 (the "Exchange Act") and, in accordance therewith, files reports and other information with the Securities and Exchange Commission (the "Commission"). Reports, proxy and information statements and other information filed by Pinnacle can be inspected and copied at the public reference facilities maintained by the Commission at 450 Fifth Street, N.W., Room 1024, Washington, D.C. 20549; Everett McKinley Dirksen Building, 219 South Dearborn Street, Room 1204, Chicago, Illinois 60604; and Jacob K. Javits Federal Building, 26 Federal Plaza, Room 1100, New York, New York 10007. Copies of such material can be obtained from the Public Reference Section of the Commission, Washington, D.C. 20549 at prescribed rates.

INCORPORATION OF CERTAIN INFORMATION BY REFERENCE

Pinnacle's Annual Report on Form 10-K for the fiscal year ended December 31, 1987, as amended on Form 8, and Pinnacle's Quarterly Report on Form 10-Q for the quarter ended March 3, 1988, heretofore filed with the Securities and Exchange Commission, are incorporated in this Prospectus by reference.

All documents filed by Pinnacle pursuant to Section 13(a), 13(c), 14 or 15(d) of the Exchange Act subsequent to the date of this Prospectus and prior to the termination of the offering of the Shares shall be deemed to be incorporated herein by reference.

Any statement contained in a document incorporated or deemed to be incorporated by reference herein shall be deemed to be modified or superseded for purposes of this Prospectus to the extent that a statement contained herein or in any other subsequently filed document which also is or is deemed to be incorporated by reference herein modifies or supersedes such statements. Any such statement so modified or superseded shall not be deemed, except as so modified or superseded, to constitute a part of this Prospectus.

Pinnacle will provide without charge to each Industries Stockholder to whom this Prospectus is delivered, upon the request of any such person, a copy of any or all of the documents incorporated by reference and described above, other than exhibits to such documents which are not specifically incorporated by reference therein. Requests should be directed to the Company at its principal executive offices, 550 Post Oak Blvd., Suite 550, Houston, Texas 77027; telephone (713) 622-8492.

INFORMATION ABOUT SELLING STOCKHOLDER

The Shares offered hereby are being sold by Industries pursuant to its Plan of Asset Redeployment, as part of its efforts to enhance liquidity while maintaining a substantial interest in the natural resources and real estate sectors. Industries believes that the offering and sale of the Shares to its stockholders is appropriate at this time to provide Industries with additional liquidity and to enable the Industries Stockholders to have the opportunity to acquire the Shares at a price deemed attractive relative to the historical price and book value of the Shares.

As of the date of this offering, Industries owns 908,571 shares of Pinnacle Common Stock (approximately 42.6% thereof), which shares represent approximately 37.7% of all the shares of Pinnacle Common Stock and Class B Common Stock outstanding, without giving effect to immediately exercisable and outstanding options or rights to purchase 743,042 shares of Pinnacle Common Stock or Class B Common Stock, or to the rights of Pinnacle Class B Common Stock which is entitled to elect a majority of Pinnacle's Board of Directors. See "Description of Pinnacle Common Stock." If all of the 400,000 shares offered hereby are purchased, Industries will own 508,574 shares (approximately 23.8%) of the shares of Pinnacle Common Stock then outstanding without giving effect to any additional issuance of shares of Pinnacle Common Stock. Industries will continue to own warrants to purchase 205,759 additional shares of Pinnacle Common Stock. The Shares offered by this Prospectus are being offered to Industries stockholders at \$0.10 per share less than the value at which the Shares are carried on Industries' balance sheet, so that, for financial reporting purposes, the sale of the Shares will result in a realized loss to Industries of approximately \$40,000 if all Shares offered are purchased.

During the last three fiscal years, Industries' only material transaction with Pinnacle was the sale by Industries in June 1985 of 111,111 shares of Pinnacle Common Stock to Pinnacle for a net purchase price of \$300,000, or \$2.70 per share. On the purchase date, Pinnacle Common Stock was reported in the over-the-counter market as \$1.50 bid and \$1.75 asked per share. The purchase price in the 1985 transaction was at a discount from the stated book value of the Pinnacle Common Stock at that time, although the price was in excess of the market prices then quoted in the over-the-counter market.

Mr. McElvenny, Industries' Chairman and Chief Executive Officer, also serves as Chairman and Chief Executive Officer of Pinnacle.

RISK FACTORS

The business of Pinnacle involves a high degree of risk. The factors discussed below should be carefully considered in evaluating Pinnacle and its business before purchasing the Shares described in this Prospectus and offered hereby:

1. Pinnacle's Business Strategy. In mid-1984, Pinnacle adopted a general business policy for future operations known as its Plan for Corporate Development (the "Plan"), which aims at expansion primarily through corporate transactions, particularly mergers, asset acquisitions, roll-ups or similar transactions. Pursuant to its corporate development objectives, during 1985, 1986

and 1987 Pinnacle acquired 100% of Spur Petroleum, Inc. ("Spur"), a privately held exploration company based in Amarillo, Texas; a majority position in Regal Petroleum, Ltd. ("Regal"), a public oil and gas exploration and production company based in Denver, Colorado; certain working interests in various proved producing oil and gas properties and undeveloped leases in Michigan from Titan Wells, Inc. ("Titan"); 100% of V-Mc Operating Co. ("V-Mc"), a privately held operating company based in Denver, Colorado; certain working interests in producing and development acreage in Osage County, Oklahoma; the oil and gas properties of five private limited partnerships managed by Centennial Petroleum Company, San Francisco, California ("Centennial Partnerships"); and certain working interests in various producing oil and gas properties located in western New York State. Pinnacle is actively evaluating other corporate development opportunities at this time. The success of Pinnacle's corporate development under the Plan is dependent in part upon factors, particularly oil and gas prices, which are beyond management's control. The ultimate success of the Plan is also highly dependent on management's ability to efficiently manage acquired properties and businesses and to negotiate acquisitions and secure financing on terms that prove to be advantageous over the long term. If Pinnacle is unsuccessful in these endeavors, the Plan for Corporate Development will not achieve growth and profitable operations.

2. Oil Prices. Since December 31, 1985, worldwide and domestic oil prices have declined dramatically. In consonance with such worldwide declines, oil prices for Pinnacle's proved oil reserves have declined significantly from an average of approximately \$27 per barrel during 1985 to an average of approximately \$14.55 in 1986 and \$17.73 in 1987, and have declined as low as \$9.50 per barrel during interim periods. Continuation for a significant period of reduced prices, or any further oil price declines, may impair Pinnacle's ability to conduct its business as presently conducted.

One material effect of dramatically lower oil prices throughout the world has been to reduce the value of oil reserves in place. The value of gas reserves has also declined dramatically. See "Gas Prices and Markets" below. To reflect the reduced reserve value of each barrel of oil or barrel equivalent unit of gas reserves in place, Pinnacle has taken substantial writedowns of reserve values. For example, in view of deteriorating conditions experienced during 1985 and the material adverse developments which have been widespread throughout the industry in recent years, Pinnacle recorded a writedown of producing properties of \$703,000 in 1986. No writedown was taken during 1987. However, if product prices decline further during 1988, Pinnacle will recognize substantial additional depreciation and depletion expenses or possible further writedowns of producing properties.

3. Gas Prices and Markets. Along with oil price declines, prices available for domestic natural gas production have experienced substantial declines in recent years. During fiscal years 1985, 1986 and 1987, Pinnacle's average sale price per Mcf of gas produced was \$3.94, \$2.32 and \$1.74, respectively. Also, gas production has faced marketing difficulties, and gas producers have found available markets restricted and terms and contract lengths materially less favorable than during past years when higher prices were obtainable for both oil and gas production.

4. Key Employees. The continued availability to Pinnacle of the services of certain key individuals engaged in the management and operation of Pinnacle are believed to be critical to Pinnacle's future success. The unexpected death or unavailability of any key executive, particularly Ralph T. McElvenny, Jr., Chairman and Chief Executive Officer of Pinnacle, for whom there is no corporate key employee life insurance, could have a detrimental effect on Pinnacle. However, it is expected that suitable employment agreements and insurance arrangements will be entered into between Pinnacle and its key executive officers in 1988.

5. Losses. Although maintaining a sound overall financial position from a balance sheet standpoint, Pinnacle has reported substantial losses in recent years. Pinnacle's reported losses include material charges or writedowns in the values of exploration acreage and oil and gas reserves required in view of declining oil and gas prices. There can be no assurance that Pinnacle will be profitable in the future as decreases in prices received by Pinnacle for its oil and gas production could result in a negative cash flow and operating losses.

6. Election of Majority of Directors and Other Rights of Holders of Class B Common Stock of Pinnacle. Pinnacle's management owns the majority of Pinnacle's currently outstanding Class B Common Stock, which has the power to elect a majority of Pinnacle's Board of Directors. In addition, Pinnacle's Class B Common Stock has the right to vote as a separate class on major corporate transactions. The Common Stock of Pinnacle being offered hereby votes share-for-share with shares of Pinnacle Class B Common Stock with respect to the election of a minority of the Pinnacle Board of Directors and on all other matters submitted to stockholders. See "Description of Pinnacle Common Stock."

7. No Cash Dividends. No cash dividends have been paid in the past to the holders of Pinnacle Common Stock, and payment of cash dividends by Pinnacle is not contemplated in the future. In 1986, the Board of Directors declared a non-cash dividend on all shares of Pinnacle Common Stock which consisted of warrants to purchase additional shares of Pinnacle Common Stock. The first exercise period for the warrants begins on September 28, 1988, and the second exercise period commences 180 days thereafter. The warrants are exercisable at \$1.00 and \$1.50 per share during the first and second exercise periods, respectively, with the exercise prices being subject to adjustment.

8. Director Liability Limitation. Pinnacle's Certificate of Incorporation implements a statute passed by the State of Delaware that permits the elimination of personal liability of directors for monetary damages for breach of fiduciary duty except for breaches of the duty of loyalty, acts or omissions not in good faith or involving intentional misconduct or knowing violation of law, and the receipt of improper personal benefit. While Pinnacle believes this director liability limitation will enhance its ability to attract and retain qualified directors, it also may limit the recourse available to stockholders if the directors were to violate their fiduciary duties.

9. Other Factors Affecting Oil and Gas Operations. Set forth below is a discussion of various further risks that affect the business and operations of Pinnacle.

Markets: The availability of a market for Pinnacle's oil and gas production depends upon numerous factors beyond its control. These factors include, but are not limited to, worldwide pricing trends and the availability of other domestic or imported production, the location and capacity of natural gas pipelines and transmission facilities, the effect of federal and state regulation on oil and gas production and general economic conditions. In addition, domestic oil and gas must compete with imported oil and gas, coal, atomic energy, hydroelectric power and other forms of energy. Excess supplies of oil and gas or these other forms of energy from time to time, including the present, have depressed prices in the oil and gas industry. In addition, the price of and demand for oil and gas is subject to, and during recent years have been materially adversely affected by, actions of foreign governments, international cartels and the United States government.

Competition in the Oil and Gas Business: Despite reduced drilling activity in recent years, the exploration for and development of oil and gas, as well as the interest in companies or properties available for sale, remain extremely competitive. In attempting to locate, acquire and develop suitable oil and gas properties, Pinnacle is competing with numerous other corporations, partnerships, individuals and other entities, including many that have significantly greater financial, technical and marketing resources.

Government Regulation: The production and sale of oil and gas are subject to federal and state government regulation in a variety of ways, including price controls and regulation concerning the prevention of waste, the conservation of oil and natural gas, pollution, and various other matters. Many jurisdictions have at various times imposed limitations on the production of oil and gas by restricting the rate of flow for oil and gas wells below their actual capacity to produce. The United States government also has the power to permit increases in the amount of oil and gas imported from other countries.

Environmental Regulation: The operations of Pinnacle are subject to numerous laws and regulations governing the discharge of materials into the environment or otherwise relating to environmental protection. These laws and regulations may require the acquisition of a permit before drilling begins, severely restrict or prohibit drilling activities on certain lands lying within wilderness areas or where environmental damage may result, impose substantial liabilities for pollution resulting from drilling operations or impose a fee or tax for other environmental impacts.

Operating Hazards and Uninsured Risks: The oil and gas operations of Pinnacle and its subsidiaries are subject to all the risks inherent in the exploration for, and development and operation of, oil and gas properties. Blowouts and fires could result in damage to or the destruction of any oil or gas well and any producing facilities. Due to the prohibitive cost of obtaining certain insurance coverages Pinnacle is not fully insured against these risks. If Pinnacle sustained an uninsured loss or liability, its ability to operate could be adversely affected.

State Regulation: State regulatory authorities have established rules and regulations requiring permits for drilling operations, drilling bonds and reports concerning operations and state taxes on production, sale and storage, or transportation of oil and gas. Most states in which Pinnacle operates also have statutes and regulations concerning the spacing of wells and environmental and conservation matters, and have established regulations to govern the unitization and pooling of properties, and to control the rate of production from oil and gas wells for the purpose of conserving oil and gas and preventing waste.

THE OFFERING

Offer to Industries Stockholders

Industries is offering to Industries Stockholders of record (the "Record Holders") at the close of business on July 20, 1988 (the "Record Date") the nontransferable right, evidenced by the Subscription Form attached as Appendix A to this Prospectus, to purchase from Industries up to an aggregate of 400,000 Shares of its Pinnacle Common Stock at the price of \$1.15 per Share (the "Subscription Price"). Pursuant to this offer, each Record Holder is entitled to purchase up to 40% of the number of shares of Industries Common Stock owned by him on the Record Date, that is, two Shares of Pinnacle Common Stock for each five shares of Industries Common Stock owned of record on the Record Date (the "Primary Subscription Right"). Record Holders should consult their personal stockbrokers or financial advisors in the event they are unable to ascertain the number of shares of Industries Common Stock owned by them as of the Record Date. Fractional Shares may not be subscribed for or purchased. To purchase Shares pursuant to the Primary Subscription Right, a Record Holder must complete and sign the Primary Subscription portion of the Subscription Form included in this Prospectus as Appendix A, and pay for the Shares subscribed for in current funds as described under "How to Subscribe."

If all 400,000 Shares offered are not sold under the Primary Subscription Rights, such remaining Shares may be subscribed for by only those participants in the Primary Subscription Right who purchased the maximum number of Shares to which they were entitled (the "Additional Subscription Right"), by completing the Additional Subscription portion of the Subscription Form in Appendix A. Under their Additional Subscription Rights, eligible Record Holders may purchase up to a maximum of the number of Shares they purchased under their Primary Subscription Rights. If more Shares are subscribed for under the Additional Subscription Rights than are available, each Record Holder will be entitled to purchase a pro rata portion of the Shares available, based upon his percentage ownership of outstanding Industries Common Stock on the Record Date. In such event, Industries will advise Record Holders who subscribed for Shares pursuant to their Additional Subscription Rights of the number of Shares they are obligated to purchase under the Additional Subscription Rights as soon as reasonably practicable following the Expiration Date. Record Holders who subscribe for Shares under the Additional Subscription Rights may pay for up to one-half of the total purchase price for such Shares by delivery of a non-recourse three-year promissory note bearing interest at ten percent (10%) per annum (the "Note"), the form of which appears in Appendix B hereto. The Note and

obligation to pay for the Additional Subscription Rights will be secured under a Collateral Assignment and Security Agreement in the form attached hereto as Appendix C by all Shares purchased by the Maker of the Note pursuant to his Additional Subscription Right under this offer.

If, following subscriptions under the Additional Subscription Rights, any Shares remain unsold, such Shares may be offered, in Industries' sole discretion, to all Industries' Stockholders who participate in this offering and who notify Industries in writing on or before the Expiration Date that they would be interested in purchasing any remaining Shares, in proportion to their percentage ownership in Industries on the Record Date. Payment for up to one-half of the purchase price for such remaining Shares may be made by delivery of a Note on the terms of the Note in Appendix B.

Some state laws contain provisions which restrict or prohibit the sale of Pinnacle Common Stock pursuant to this offering including the states of California and Texas.

Offer Expiration Date

This offer will expire at 3:00 p.m. Mountain time on August 31, 1988 (the "Expiration Date"), if not previously extended at the sole discretion of Industries. Mountain States Stock Transfer Agents, Inc. (the "Subscription Agent") must receive the Subscription Form, together with payment in full of the Subscription Price for all Shares purchased upon the exercise of Primary Subscription Rights, at 1777 South Harrison Street, Penthouse Suite P207, Denver, Colorado 80210, on or before the Expiration Date, except as otherwise noted below (see "How to Subscribe - Late Delivery of Subscription Forms"). No Primary Subscriptions received after the Expiration Date can be accepted.

Plan of Solicitation

The offer to the Record Holders will be made through Industries' officers, directors and employees and no commission or any form of remuneration in addition to their regular salaries will be paid to them for making the offer. In addition, Industries may retain broker/dealer firms to solicit subscriptions from Industries Stockholders for a fee of up to \$7,500. After this Prospectus and the Subscription Form have been mailed to Record Holders, subscriptions may be solicited by the mails, telephone and personal contacts by officers, directors and other employees of Industries, or by any broker/dealer or other solicitation firms retained by Industries.

HOW TO SUBSCRIBE

Primary Subscription Rights

A Subscription Form is included in the back of this Prospectus at Appendix A. To exercise their Primary Subscription Rights, Record Holders should complete and sign the Subscription Form and mail or deliver it to the Subscription Agent, Mountain States Stock Transfer Agents, Inc., 1777 South Harrison Street, Penthouse Suite P207, Denver, Colorado 80210, together with payment in full for all Shares for which the holder has subscribed pursuant to the

Primary Subscription Right. Personal checks will be accepted as payment. The payment and Subscription Form must be received by the Subscription Agent before 3:00 p.m., Mountain Time, on the Expiration Date, unless such date is extended by Industries in its sole discretion. The rights evidenced by the Subscription Form may not be transferred. See "Payment and Other Matters" below.

Additional Subscription Rights

To be eligible to purchase Shares under the Additional Subscription Right, a Record Holder must subscribe for the maximum number of Shares available to him under the Primary Subscription Right (that number of shares of Pinnacle equal to 40% of the number of shares of Industries owned by the Record Holder as of the Record Date), and complete the Additional Subscription Rights portion of the Subscription Form at the time his Primary Subscription Right is exercised. A Record Holder may purchase under the Additional Subscription Right up to a maximum of the number of Shares purchased under the Primary Subscription Right. A Record Holder may indicate on the Subscription Form that he desires to subscribe for a specified number of Shares which may be less than the maximum number to which such Record Holder is entitled. If more Shares are subscribed for pursuant to the Additional Subscription Rights than are then available, the total number of available Shares will be allocated pro rata among those exercising their Additional Subscription Rights in proportion to their percentage ownership in Industries on the Record Date. Any questions as to the allocation of Additional Subscription Rights will be determined by Industries within its sole discretion, and such decision will be binding upon all Record Holders.

Promptly after making the allocation of additional Shares, Industries will notify each Record Holder exercising Additional Subscription Rights of the number of Shares that such holder is thereby obligated to purchase. The Subscription Price for Shares purchased pursuant to the Additional Subscription Rights must be received by the Subscription Agent no later than 3:00 p.m. Mountain time on September 16, 1988, or, if the Expiration Date has been extended, within 20 business days after such extended date.

If, following subscriptions under the Additional Subscription Rights, any Shares remain unsold, such Shares may, in Industries' sole discretion, be offered to any Industries Stockholders who participate in this offering and who notify Industries in writing on or before the Expiration Date that they would be interested in purchasing any remaining Shares, in proportion to their percentage ownership in Industries on the Record Date. Payment for up to one-half of the purchase price for such remaining Shares may be made by delivery of a Note on the terms of the Note in Appendix B.

Payment and Other Matters

The Primary Subscription Price must be received by the Subscription Agent no later than the Expiration Date. Full payment must be made by check, bank draft, wire transfer or postal or express money order payable in United States dollars to the order of "MOUNTAIN STATES STOCK TRANSFER AGENTS, INC." Payment of the current funds portion of the Additional Subscription Price must be made in the same manner and received by the Subscription Agent no

later than 3:00 p.m., Mountain Time, on September 16, 1988. If applicable, an executed Note representing the remaining portion of the Additional Subscription Price and an executed Collateral Assignment and Security Agreement must be delivered to the Subscription Agent at the same time as the payment of the cash portion of the Subscription Price.

Once a Record Holder has exercised his Primary or Additional Subscription Rights, the exercise is irrevocable. Subscriptions must be for full Shares only. If the Record Holder's payment is less than that required to purchase the number of Shares subscribed for, Industries will sell only the number of Shares for which payment is received. Certificates representing the Shares of Pinnacle's Common Stock will be issued as soon as practicable after receipt of payment therefor.

The instructions on the Subscription Form should be read carefully and followed in detail. The risk of delivery of Subscription Forms and payments will be borne by the Record Holders and not by Industries. If the mail is used to exercise rights, it is recommended that insured, registered mail be used. Any questions or requests for assistance concerning the method of subscribing, or for additional copies of this Prospectus, should be directed to the Subscription Agent.

All questions as to the validity, form, eligibility and acceptance of any exercise of rights will be determined by Industries. Industries may waive any irregularity or defect, permit any irregularity or defect to be corrected within such time as it may determine, or reject any subscription that it determines has not been made properly.

Delivery of Subscription Forms and Payments

Subscription Forms and payments of the Subscription Price should be mailed or delivered to the Subscription Agent at its address below:

Mountain States Stock Transfer Agents, Inc.
1777 South Harrison Street
Penthouse Suite P207
Denver, Colorado 80210
Attention: Stacie Scott

The Subscription Agent's telephone number is (303) 759-2441. Ms. Laura Sisneros or Ms. Stacie Scott will be available at that number to contact concerning questions or instructions in connection with this offer.

Late Delivery of Subscription Forms

If on or before the Expiration Date Industries receives the Subscription Price by wire transfer or otherwise together with a letter or telegram from a bank, trust company or member firm of the National Association of Securities Dealers, Inc. stating the name of the subscriber and the number of Shares subscribed for and guaranteeing the delivery of the executed Subscription Form within five business days of the Expiration Date, the subscription will be accepted subject to receipt of the duly executed Subscription Form within five business days.

Subscription Proceeds

All funds received by the Subscription Agent from the exercise of rights will be held by the Subscription Agent until the Expiration Date. If the offering is cancelled or terminated for any reason, the Subscription Agent will return to each subscriber all funds held for his or her own account. No interest will be paid on funds returned due to cancellation of the offering or otherwise.

Participation by Industries' Board of Directors

All of the directors of Industries, including Ralph T. McElvenny, Jr., who is Chairman and Chief Executive Officer and a principal stockholder of both Industries and Pinnacle, have advised that they intend to purchase the maximum number of Shares available pursuant to their Primary Subscription Rights, and Mr. McElvenny has also advised that he intends to purchase the maximum number of Shares for which he may be eligible under the Additional Subscription Rights. Mr. McElvenny has further advised that he is likely to participate as an interested stockholder in the purchase of any unsold Shares.

Determination of Subscription Price

The Subscription Price has been determined by the Board of Directors of Industries based upon consideration of a number of factors, including (1) the bid and asked prices of the Pinnacle Common Stock; (2) Pinnacle's current financial position (including its earnings history and stockholders' equity); (3) the estimated price at which Record Holders would likely be willing to exercise their Subscription Rights; (4) the uncertainties regarding the oil and gas industry in general and Pinnacle's oil and gas exploration and development activities in particular; (5) the prices and discounts from market prices at which similar offerings have been effected; and (6) the non-transferable nature of the rights.

Federal Income Tax Matters Relating to the Offering

Pinnacle believes that the receipt of the right by the Industries Stockholders to purchase Pinnacle Common Stock pursuant to this offer should not give rise to federal income tax liability, because the right of an Industries Stockholder to acquire the Shares offered hereby is itself only of nominal or no monetary value in view of factors including the offering price and market price history of Pinnacle Common Stock; the non-transferability of the right; and the limited period during which the right is exercisable. However, if the right were deemed to be of more than merely nominal value, Industries has been advised that the fair market value of the right would be treated as a taxable dividend upon receipt to the extent that it is out of current or accumulated earnings and profits of Industries. Also, an Industries Stockholder's basis in his Industries Common Stock would be reduced by the value of the right received to the extent not treated as a taxable dividend, and an Industries Stockholder who did not exercise his right could claim a short-term capital loss equal to the fair market value of such right. The exercise of a right should not be a taxable event for federal income tax purposes. However, all Industries Stockholders should consult their personal tax advisor to discuss the possible tax consequences of this offer.

Industries Stockholders whose payment for the purchase of additional Shares includes delivery of a Note pursuant to their Additional Subscription Rights should be aware that the interest paid on the Note may be of limited deductibility due to the investment interest limitations under the new federal tax laws.

USE OF PROCEEDS

All of the Shares of Pinnacle Common Stock offered hereby are being sold for the account of Industries and the proceeds will be used for general corporate purposes. If all of the shares offered hereby are purchased, Industries will net proceeds of approximately \$420,000 after payment of an estimated \$40,000 in offering expenses. Pinnacle will not receive any of the proceeds of this offering.

PRICE RANGE OF PINNACLE COMMON STOCK

Pinnacle Common Stock is traded in the over-the-counter market. The following table shows, for the calendar quarters indicated, the reported high and low bid quotations for Pinnacle Common Stock. Quotations are as reported by the National Association of Securities Dealers Automated Quotation System, the National Quotation Bureau or members of the National Association of Securities Dealers who maintain a market in Pinnacle's shares. Such quotations represent prices between dealers without retail markup, markdown or commissions and do not necessarily represent actual transactions. The closing bid and asked prices on July 29, 1988, were \$1.125 and \$1.375, respectively.

<u>Quarter Ended</u>	<u>High</u>	<u>Low</u>
<u>1988</u>		
March 31	\$1.375	\$1.250
June 30	1.250	1.063
<u>1987</u>		
March 31	1.188	1.063
June 30	1.375	1.188
September 30	1.438	1.250
December 31	1.375	1.250
<u>1986</u>		
March 31	1.500	1.375
June 30	1.500	1.375
September 30	1.500	1.375
December 31	1.375	1.250

BUSINESS OF PINNACLE

The following is a brief description of the general business of Pinnacle and a summary of the activities of Pinnacle subsequent to the period covered by its Annual Report on Form 10-K for the year ended December 31, 1987. For a more complete description of the business, properties and activities of Pinnacle, see Pinnacle's Annual Report on Form 10-K for the year ended December 31, 1987 and the documents listed under "Incorporation of Certain Information by Reference."

General

Pinnacle, a publicly-owned oil and gas exploration and production company, owns slightly in excess of 50% of the shares of voting common stock of Regal Petroleum, Ltd., also a publicly-owned oil and gas company. At December 31, 1987, on a consolidated financial reporting basis, Pinnacle had cash and equivalent items in excess of \$2,900,000 and no bank indebtedness. Due to lower product prices, Pinnacle wrote down the value of its oil and gas properties by \$703,000 during 1986. However, Pinnacle's management believes that, in view of factors including Pinnacle's overall liquidity position and unused borrowing capacity, Pinnacle remains well positioned to pursue its corporate development objectives. Pinnacle's growth objectives include the use of Pinnacle Common Stock to acquire partnerships and corporations through mergers, exchange offers and similar transactions, while maintaining adequate liquidity for development or other needs and opportunities.

Summary Financial Information. During 1987, Pinnacle increased its proved oil and gas reserves from the prior year-end report of December 31, 1986. Also at December 31, 1987, on a consolidated financial reporting basis, Pinnacle had total net cash and other current assets of approximately \$3,500,000, and total current liabilities of approximately \$697,118. Pinnacle's majority owned affiliate, Regal, is also publicly traded. Neither company has bank indebtedness.

The condensed consolidated balance sheet and consolidated statement of operations of Pinnacle at December 31, 1987, is as shown below. Additional information as to Pinnacle's reserves is set forth thereafter under "Summary Reserve Information."

Condensed Consolidated Balance Sheet at December 31, 1987

Cash and short term	\$2,968,466	Accounts payable	\$ 667,673
Accounts receivable, net	415,539	Accrued expenses	89,445
Note receivable-stockholder	125,000	Total current	
Prepaid expenses and other	66,196	liabilities	697,118
Total current assets	3,518,141	Minority interest - Regal	1,357,649
Oil and gas properties	4,347,362	Stockholders' equity	3,892,316
Pipeline and equipment	476,481		
	4,823,843		35,946,477
Less accumulated depreciation and impairment reserve	(2,469,327)		
Net Property	2,354,516		
Cost in excess of net assets acquired, net	78,326		
	<u>\$5,946,477</u>		

Condensed Consolidated Statement of Operations

	Twelve Months Ended December 31,	
	1987	1986
Revenues:		
Oil and gas production	\$ 725,123	669,811
Interest income	254,630	335,880
Gain on sale of property and equipment	9,340	68,690
Other	45,615	21,716
Total revenues	<u>1,629,168</u>	<u>1,634,691</u>
Costs and expenses:		
Production costs	482,362	473,736
Depreciation, depletion and amortisation	573,918	966,766
Impairment reserve on non-producing properties	86,292	88,977
Inventory valuation reserve	--	47,974
Dry hole costs and abandonments	26,520	264,290
General and administrative	842,222	1,579,621
Writedown of producing properties	--	763,000
Amortisation of cost in excess of net assets acquired	19,765	--
Total costs and expenses	<u>2,619,619</u>	<u>4,658,364</u>
Earnings (loss) from operations	(989,911)	(3,024,273)
Minority interest in net loss of Regal Petroleum, Ltd.	203,950	923,560
Net earnings (loss)	<u>\$ (785,961)</u>	<u>(2,100,713)</u>
Net earnings (loss) per common share (after preferred dividends of \$25,000 in 1987 and \$63,187 in 1986)	<u>\$ (.35)</u>	<u>(1.12)</u>
Weighted average number of common shares outstanding	<u>2,333,222</u>	<u>1,937,615</u>

The condensed consolidated financial statements should be read in conjunction with Pinnacle's Annual Report on Form 10-K incorporated herein by reference.

Summary Reserve Information. Bradbury Engineering Group, Inc., Friendswood, Texas, independent petroleum engineers, prepared the estimated reserve information for Pinnacle and Regal for the years ended December 31, 1987 and 1986, showing estimated future revenues based on the prices in effect at the close of the respective fiscal years.

The following table sets forth the estimated net quantities of proved and proved developed oil and gas reserves as of the indicated dates and prices then in effect:

<u>As of</u>	<u>Proved Reserves</u>		<u>Proved Developed Reserves</u>	
	<u>Oil(Bbls)</u>	<u>Gas(Mcf)</u>	<u>Oil(Bbls)</u>	<u>Gas(Mcf)</u>
December 31, 1987 ¹	155,581	1,158,198	148,951	988,885
December 31, 1986 ²	181,429	592,791	94,888	589,825
December 31, 1985 ³	193,577	928,943	188,815	915,998

¹ Proved Reserves include 45,798 barrels and 235,822 Mcf and Proved Developed Reserves include 45,798 and 192,222 Mcf of reserves attributable to the minority interest in Regal Petroleum, Ltd.

² Proved and Proved Developed Reserves include 41,516 barrels and 212,348 Mcf of reserves attributable to the minority interest in Regal Petroleum, Ltd.

³ Proved and Proved Developed Reserves include 86,736 barrels and 352,686 Mcf of reserves attributable to the minority interest in Regal Petroleum, Ltd.

Present Value of Estimated Future Net Revenues. The present value of estimated future net revenues of proved and proved developed reserves of the Company at the dates indicated below was computed according to SEC reporting requirements by discounting the aggregate estimated future net revenues by 10% per year. The present value is not believed to represent the fair market value of the reserves either as of the year end or as of the date hereof.

<u>As of</u>	<u>Proved Reserves</u>	<u>Proved Developed Reserves</u>
December 31, 1987 ¹	\$ 1,938,942	\$ 1,748,523
December 31, 1986 ²	1,318,758	1,288,489
December 31, 1985 ³	3,691,742	3,495,439

¹ Includes the present value of estimated future net revenues of proved and proved developed reserves of \$587,818 and \$473,698, respectively, attributable to the minority interest in Regal Petroleum, Ltd.

² Includes the present value of estimated future net revenues of proved and proved developed reserves of \$488,858 attributable to the minority interest in Regal Petroleum, Ltd.

³ Includes the present value of estimated future net revenues of proved and proved developed reserves of \$1,853,215 attributable to the minority interest in Regal Petroleum, Ltd.

Expansion Strategy. In July 1984, Pinnacle's newly elected management formulated the Plan, a general outline of objectives to guide the development of the Company for the foreseeable future. The Plan provides generally that Pinnacle should expand primarily through corporate transactions, particularly

merger, acquisition, roll-up or like transactions. In seeking expansion under the Plan, management intends to preserve a sound financial position so as to enhance Pinnacle's choice of options and its flexibility in structuring and participating in further transactions. Under the Plan, Pinnacle anticipates that it will emphasize growth through corporate transactions, rather than through "wildcat" or straight exploration drilling participations in a relatively limited number of exploration prospects. Pinnacle regularly reviews, participates in or manages development exploration and operations. As a general guideline, in order to spread exploration and development risks, Pinnacle seeks to limit its percentage participation in any single project to a range of from 25% to 50% of the total available participation.

While expanding operations, Pinnacle intends to remain alert to corporate development opportunities and is regularly engaged in active discussions with candidates for potential business combinations. At this time no agreement has been reached with any such candidates; however, active investigation and discussions are continuing. Management believes that recent oil price volatility as well as the fragmented nature of the independent exploration industry, its generally depressed condition and other adverse factors may increase the variety and number of corporate transactions available to Pinnacle for review.

Pursuant to the corporate development strategy envisioned in the Plan, principal transactions have been completed as discussed and summarized below:

Regal Acquisition. On September 25, 1985, PinReg Corporation ("PinReg"), a newly formed, wholly-owned Delaware subsidiary of the Company, purchased 2,025,600 shares of Regal Petroleum, Ltd. ("Regal") common stock, par value \$.01 per share. Such shares were purchased for total consideration of \$1,114,080 from nine Regal stockholders, and the Company agreed to purchase 4,996,585 shares of Regal common stock in a private placement. Through December 31, 1985, PinReg purchased 507,915 additional shares in open market and private transactions. As a result of these purchases PinReg owns 7,500,100 shares, or slightly in excess of 50.0% of Regal's outstanding common stock.

A plan for a business combination of Pinnacle and Regal has been discussed between each company's management, although the structure and terms of such combination have not yet been resolved. Because of the uncertainty as to structure and terms, Pinnacle's management is unable to predict whether such combination will result in any dilution of Pinnacle's earnings per share or dilution in the book value of outstanding Pinnacle Common Stock.

Spur Acquisition. Pursuant to an agreement dated November 27, 1985, between PinSpur Corporation, a newly formed, wholly-owned Texas subsidiary of Pinnacle, and Spur Petroleum, Inc. ("Spur"), a privately held Texas corporation based in Amarillo, Texas, Pinnacle acquired by merger, all of the outstanding common stock of Spur on December 27, 1985. In that transaction, Spur stockholders were issued 176,415 unregistered shares of Pinnacle Common Stock. Spur owns working interests in producing oil and gas leases in Texas and Oklahoma as well as approximately 20,000 gross acres of undeveloped exploration leases in Deaf Smith County, Texas.

Titan Acquisition. On June 28, 1985, Pinnacle issued to Titan Wells, Inc., whose principal stockholder is Pinnacle's Chairman, 675,000 shares of Series A

Convertible Voting Preferred Stock ("Series A Preferred Stock"), together with warrants to purchase up to 200,000 shares of Pinnacle Common Stock through December 1990. In consideration of the issuance of such Series A Preferred Stock and the warrants, Pinnacle received from Titan \$450,000 cash, working interests in various proved producing oil and gas properties and certain undeveloped leases in Michigan. In November 1987, Pinnacle redeemed all of the remaining Series A Preferred Stock outstanding for a net price of \$436,500.

V-Mc Acquisition. On March 10, 1987, Pinnacle acquired V-Mc Operating Co. ("V-Mc"), an oil and gas operating company, under a Stock Purchase Agreement (the "V-Mc Agreement") by and among Pinnacle, and V-Mc's stockholders. Under the V-Mc Agreement, V-Mc became a wholly-owned subsidiary of Pinnacle and the former V-Mc stockholders received 100,000 unregistered shares of Pinnacle Common Stock.

In a separate transaction also effective as of March 10, 1987, Pinnacle (through a wholly-owned subsidiary) acquired various producing oil and gas working interests from V-Mc's former stockholders and certain related parties in exchange for an aggregate of 58,569 unregistered shares of Pinnacle Common Stock.

Centennial Acquisition. During April 1987, Pinnacle (through a wholly-owned subsidiary) acquired certain privately held oil and gas working interests owned by Centennial 2nd 1981 Drilling Program, Centennial 3rd 1981 Drilling Program, Centennial 1st 1982 Drilling Program, Centennial 2nd 1982 Drilling Program, and Centennial 1st 1983 Drilling Program (together, the "Centennial Partnerships"). Centennial Petroleum Company, a California partnership, acted as general partner (the "General Partner") for all of the Centennial Partnerships, and Mr. John C. Roberts served as the sole general partner of the General Partner. The subject oil and gas working interests acquired by Pinnacle are located in Oklahoma, Kansas, Wyoming and New York. Under terms of the acquisition, the Centennial Partnerships received as consideration in exchange for the working interests conveyed to Pinnacle an aggregate of 148,983 unregistered shares of Pinnacle Common Stock.

Acquisition of Working Interests in New York State. Effective September 1, 1987, Pinnacle and Regal acquired, respectively, certain working interests in shallow gas properties located in western New York State. The interests were purchased from the Phelps Dodge Corporation for cash consideration of \$229,500.

Transactions with Management

Future loans to Pinnacle's officers, affiliates and/or shareholders will be approved by a majority of the disinterested directors and transactions with affiliates will be on terms no less favorable than could be obtained from unaffiliated parties.

DESCRIPTION OF PINNACLE COMMON STOCK

Pinnacle has outstanding Common Stock and Class B Common Stock, and warrants and options to purchase Common Stock or Class B Common Stock.

Pinnacle Common Stock (the class of shares being offered by this Prospectus) has all of the voting and other rights customary for common stock, except that it is entitled to vote on the election of only a minority of the Board of Directors, in which the Pinnacle Common Stock votes share-for-share with the Class B Common Stock. The Class B Common Stock has the right, voting as a separate class, to elect a simple majority of the Board of Directors, and to vote as a separate class on certain other major corporate transactions, such as mergers or liquidations. A majority of the Class B Common Stock is owned by Pinnacle's management. Pinnacle Common Stock also votes share-for-share with the Class B Common Stock on all other matters.

ADDITIONAL INFORMATION

Pinnacle has filed with the Securities and Exchange Commission, 450 Fifth Street N.W., Washington, D.C. 20549, a Registration Statement under the Act with respect to the Shares offered hereby. This Prospectus does not contain all of the information set forth in the Registration Statement and the exhibits and schedules thereto. For further information with respect to Pinnacle and the Shares, reference is hereby made to such Registration Statement, exhibits and schedules.

LEGAL OPINION

Certain legal matters in respect of the Shares offered hereby will be passed upon for Pinnacle by Davis, Graham & Stubbs, 370 Seventeenth Street, Denver, Colorado 80202.

EXPERTS

The consolidated financial statements and related financial statement schedules in Pinnacle's Annual Report on Form 10-K for the year ended December 31, 1987, have been examined by Coopers & Lybrand, independent certified public accountants, as set forth in their report dated March 25, 1988, and are incorporated herein by reference in reliance upon the authority of said firm as experts in auditing and accounting.

The summary reserve information relating to the Company's oil and gas reserves presented under the heading "Business of Pinnacle - General - Summary Reserve Information" was derived from the report on Estimate of Proved Reserves Attributable to Pinnacle Petroleum, Inc., prepared by Bradbury Engineering Group, Inc., Friendswood, Texas, dated as of January 1, 1988, and is included herein in reliance upon the authority of said firm as experts in petroleum engineering.

INSTRUCTIONS ON HOW TO SUBSCRIBE

PRIMARY SUBSCRIPTION RIGHTS

- Total of 400,000 shares of Pinnacle Common Stock available.
- Each Record Holder may purchase a maximum of up to that number of Shares of Pinnacle Common Stock equal to 40% of the number of shares of Industries Common Stock he owned as of July 20, 1988 (that is, 2 shares of Pinnacle for every 5 shares of Industries).
- Indicate number of Shares desired on the Primary Subscription Form and amount to be paid (at \$1.15 per share).
- Payment for all Shares purchased under the Primary Subscription Rights must be in cash and must be received with the Primary Subscription Form on or before August 31, 1988.

ADDITIONAL SUBSCRIPTION RIGHTS

- Available only to Record Holders who purchased the maximum number of Shares of Pinnacle Common Stock available to them under the Primary Subscription Rights.
- At time of filling out the Primary Subscription Form, indicate the number of Shares desired on the Additional Subscription Form, up to a maximum of the number of Shares purchased under the Primary Subscription Rights.
- Record Holders who subscribe for Shares under the Additional Subscription Rights will be advised as soon as practicable following the Expiration Date of the number of Shares they are obligated to purchase under the Additional Subscription Rights and the amount of payment required.
- Record Holders who subscribe for Shares under the Additional Subscription Right may deliver a Note in payment for up to one-half of the purchase price of such Shares. Alternatively, full cash payment will be accepted.
- If more Shares are subscribed for than are available, available Shares will be allocated among subscribers pro rata based on their percentage ownership of Industries on July 20, 1988.
- Payment for all Shares purchased under the Additional Subscription Right must be received on or before September 16, 1988.

UNSOLD SHARES

- Industries may offer to interested stockholders any Shares remaining unsold following subscriptions under the Additional Subscription Rights.
- Industries Stockholders who would be interested in purchasing any such unsold Shares should so notify Industries in writing on or before August 31, 1988.
- Payment for up to one-half of the purchase price of any such remaining Shares may be made by delivery of a Note.

GENERAL INFORMATION

- All Subscription Forms and payments should be mailed to:
Mountain States Stock Transfer Agents, Inc.
1777 South Harrison Street
Penthouse Suite P207
Denver, Colorado 80210
Attn: Ms. Stacie Scott
- Subscriptions constitute legally binding obligations to purchase all Shares subscribed for under Primary and Additional Subscription Rights.

**USR INDUSTRIES, INC.
Subscription Form for Shares
of Pinnacle Petroleum, Inc.**

Name of Subscriber and
number of Shares of USR Industries, Inc.
owned by Subscriber as of
Record Date:

The Subscriber named above hereby subscribes from USR Industries, Inc., as a Primary Subscription Right, for the number of shares of Common Stock of Pinnacle Petroleum, Inc. noted below at a purchase price of \$1.15 per share. Additionally, the Subscriber hereby subscribes from USR Industries, Inc. for the number of additional shares of Common Stock noted below, as an Additional Subscription Right, upon the terms and subject to the conditions specified in the Prospectus relating to the shares offered.

Share certificates will be mailed as soon as practicable after subscription. No fractional shares may be subscribed for or purchased.

PRIMARY SUBSCRIPTION

(Each Stockholder of USR Industries, Inc. is entitled to purchase
up to two shares of Pinnacle Petroleum, Inc. Common Stock
for each five shares of USR Industries
Common Stock he holds of record on July 20, 1988)

Number of shares subscribed
to pursuant to Primary
Subscription Right: _____

Subscription Price enclosed (\$1.15 per share
times number of shares subscribed for): _____

(Make payable to "Mountain States Stock Transfer Agents, Inc.")

ADDITIONAL SUBSCRIPTION

(Stockholders who subscribed for all Shares available to them under their Primary Subscription Right may subscribe for a portion of the additional Shares, if any, which are not subscribed for by the exercise of Primary Subscription Rights, up to a maximum of the number of Shares subscribed by them for under their Primary Subscription Right.)

Number of shares subscribed
to pursuant to Additional
Subscription Right:

_____ Shares

Payment. You will be notified promptly after the Expiration Date of the number of additional shares you are obligated to purchase under your Additional Subscription Right. All Shares subscribed for pursuant to the Additional Subscription Right must be paid for on or before September 16, 1988, by delivery to Mountain States Stock Transfer Agents of the payment of current funds and Note (if applicable) constituting the Additional Subscription Price. Checks should be made payable to "Mountain States Stock Transfer Agents, Inc." with simultaneous delivery to Mountain States of an executed Note and Collateral Assignment and Security Agreement, if applicable.

**BY EXECUTING BELOW, THE UNDERSIGNED INTENDS TO
BECOME LEGALLY BOUND TO PURCHASE THE SHARES
SUBSCRIBED FOR ON THIS FORM.**

Subscriber's Signature: _____

Joint Signature (if applicable): _____

Social Security or Tax I.D. No. _____

Address (including
zip code) _____

Telephone Number: _____

MAIL TO: MOUNTAIN STATES STOCK TRANSFER AGENTS, INC.
Penthouse Suite P207
1777 South Harrison Street
Denver, Colorado 80210
Attention: Stacie Scott

**NOTE: PAYMENTS FOR SHARES PURCHASED UNDER
PRIMARY SUBSCRIPTION RIGHTS HEREUNDER MUST BE RECEIVED
PRIOR TO AUGUST 31, 1988, UNLESS THE OFFERING DEADLINE IS
EXTENDED. THE RIGHTS REPRESENTED BY THIS FORM ARE NOT TRANSFERABLE.**

PROMISSORY NOTE

\$ _____ Dated this _____ day of _____, 1988.

FOR VALUE RECEIVED, the undersigned, _____ (the "Maker"), hereby promises to pay to the order of USR Industries, Inc., a Delaware corporation (the "Payee"), at the principal office of the Payee in Houston, Texas, on _____, 1991, the principal amount of _____ Dollars (\$ _____). The outstanding balance of this Note shall bear simple interest at 10% per annum commencing on the date of this Note, and accrued interest shall be payable on the first, second and third anniversaries of the date hereof.

1. This Note is secured by certain of the Maker's shares of Common Stock, \$.01 par value, of Pinnacle Petroleum, Inc. purchased by Maker from Payee (the "Shares"), pursuant to a Collateral Assignment and Security Agreement of even date herewith, which security interest may be, but is not required to be, perfected by the Payee by taking into its possession the certificates representing such Shares.

2. This Note may be prepaid at any time without penalty.

3. If Maker fails to pay any amount that he is required to pay under this Note on or before the date when such amount is due and payable, he shall be deemed to be in default hereunder. Upon such a default, the full amount of the outstanding balance of this Note and all interest accrued thereon shall become immediately due and payable and shall bear simple interest at 18% per annum from the date of default until the date of payment in full of all amounts due and owing under this Note. Upon any such default not cured within the sixty (60) days from notice thereof, the Payee shall have:

(i) all of the rights granted to it under the Collateral Assignment and Security Agreement executed by Maker in connection with his purchase of the Shares from the Payee;

(ii) the right to sell the Shares of the Maker at public or private sale, in which event the Maker shall be liable to Payee for the amount in default hereunder, plus interest and all costs and expenses of collection, foreclosure and sale, including, without limitation, reasonable attorneys' fees; and

(iii) the right to require the Maker to unconditionally and irrevocably assign all of his Shares to any person or entities selected by the Payee, which persons or entities may include those related to or affiliated with the Payee.

4. The Maker hereby assents and agrees to any extension of time with respect to any payment due under this Note, to any partial payments, to any substitution or release of collateral, and to the addition or release of any party

liable hereon, before, at or after maturity, and such consent shall not release, alter, or diminish the liability of the Maker under this Note.

5. There shall be no personal liability to Maker to pay the indebtedness evidenced by this Note or for the performance of any of the terms, conditions or covenants expressed herein or in the Collateral Assignment and Security Agreement pursuant to which this Note is secured; provided, however, that in the event of default hereunder or under the Collateral Assignment and Security Agreement, recourse shall be had only against the Collateral (as defined in the Collateral Assignment and Security Agreement), and in any action or proceeding brought on this Note or under the Collateral Assignment and Security Agreement, no deficiency or other money judgment shall be sought or obtained, and no cause of action shall lie, against Maker whether or not he is personally liable. It is further understood and agreed, however, that nothing contained in this paragraph shall in any manner or way affect or impair (i) the existence of the nonrecourse indebtedness evidenced by this Note; (ii) the enforceability of the lien and security interest created by the Collateral Assignment and Security Agreement; or (iii) the right to name Maker as a defendant in any action instituted solely to foreclose the lien created by the Collateral Assignment and Security Agreement and divest Maker of title to the Collateral.

6. This Note is non-negotiable.

Name(s) of Maker
(Please Print or Type)

Signature(s) of Maker

COLLATERAL ASSIGNMENT AND SECURITY AGREEMENT

THIS COLLATERAL ASSIGNMENT AND SECURITY AGREEMENT is entered into this _____ day of _____, 1988 between (the "Assignor") and USR Industries, Inc., a Delaware corporation ("Industries").

RECITAL:

Either prior to or simultaneously with the execution hereof, the Assignor has executed a Subscription Form, pursuant to which the Assignor has subscribed pursuant to his Additional Subscription Rights to purchase from Industries (insert total number of shares purchased under Additional Subscription Rights) shares of the Common Stock, \$.01 par value, of Pinnacle Petroleum, Inc. (the "Shares"). In addition to the Subscription Form, the Assignor has executed a promissory note (the "Note") in favor of Industries to pay the purchase price of some of the Shares. The Assignor is required to assign as collateral (as hereafter defined) to or for the benefit of Industries (hereinafter sometimes referred to as the "Assignee") the Shares purchased by Assignor from Industries to secure payment on the Note made by the Assignor.

Accordingly, for good and valuable consideration, the receipt and sufficiency of which is hereby acknowledged, the parties agree as follows:

1. Assignment. The Assignor hereby assigns, transfers and sets over to the Assignee all of the Assignor's Shares (the "Collateral"). The assignment, transfer and setting over of the Collateral (exclusive of the right of Assignee to vote the Shares) is being undertaken by the Assignor to provide security for the performance of all terms, conditions and covenants expressed in the Note and this Collateral Assignment and Security Agreement.

2. Warranties and Covenants. The Assignor hereby represents, warrants and covenants that now and at the time of acceptance of his subscription for Shares, except for the assignment made hereby, he is the owner of the Collateral free and clear of any lien, security interest or other encumbrance and will not permit the same to be placed upon the Collateral or permit the Collateral to be attached or replevied; and that the Assignor will not sell, transfer, assign or dispose of all or any part of the Collateral or any interest therein; and that Assignor will pay all taxes and assessments of every nature or kind which may be levied or assessed against the Collateral.

3. Events of Default. The Assignor shall be in default hereunder upon the occurrence of any of the following events or conditions which shall not have been cured within sixty (60) days of notice thereof:

(a) default in the performance of any obligation contained herein or default in the payment or performance of any obligation set forth in the Note;

(b) the sale, assignment, transfer or encumbrance of any of the Collateral by the Assignor or the making of any levies, seizures or attachments thereof; or

(c) the insolvency or business failure or the assignment for the benefit of creditors or the commencement of any proceeding under any bankruptcy act or insolvency law by the Assignor.

So long as there is no default by the Assignor, the Assignor may receive all dividends paid on the Shares and may exercise his voting and other rights under the Shares, and no such action by the Assignor shall be considered a default hereunder.

4. Effect of Default. Upon default hereunder and at any time thereafter, all distributions of any kind or nature to which Assignor is entitled with respect to the Shares shall belong to and be paid to the Assignee, as its interest may appear, to be applied against the indebtedness to the Assignee secured hereby. The Assignee will also, upon any default, have the following rights:

(a) the remedies of a secured party under the Uniform Commercial Code to the extent adopted in the State of Texas at V.T.C.A., Bus. & C. § 1-101, et seq., and such other provisions of Texas law as may now be or hereafter become applicable, and the right to foreclose, sell and dispose of the Collateral in accordance with the provisions thereof. The Assignee will give the Assignor reasonable notice of the time and place of any public sale of the Collateral or of the time after which any private sale of the Collateral or any other intended disposition thereof is to be made. The requirement of reasonable notice set forth above shall be met if such notice is mailed postage prepaid, return receipt requested and sent to the address of the Assignor identified below at least ten (10) calendar days before the time of the sale or disposition. The Assignor hereby acknowledges and agrees that any such public or private sale by the Assignee shall be deemed to be a transaction executed by a bona fide pledgee without any purpose of evading any applicable securities law. The proceeds of disposition of the Collateral shall be applied first to the reasonable expenses of taking possession, holding, preparing for sale and selling the Collateral, second, to the indebtedness secured hereby and the remainder, if any, shall be paid to the Assignor;

(b) the right to require the Assignor, provided his default shall not have been cured within sixty (60) days of notice of such default, to unconditionally and irrevocably assign his Shares to any person or entities selected by the Assignee, which persons or entities may include those related to or affiliated with the Assignee; provided, however, that if the value of the Shares assigned exceeds the reasonable expenses of taking possession, holding and assigning such Shares and the indebtedness secured hereby, the Assignee shall pay over to the Assignor an amount equal to such excess in accordance with Texas law. For purposes of this Section 4(b), the value of the Shares assigned shall be deemed to be the last sale price reported for the Common Stock of Pinnacle Petroleum, Inc. by the principal exchange on which such stock is traded, at the

close of trading on the last trading day immediately preceding such assignment, or if unavailable, then the last bid price reported as of such date by the National Association of Securities Dealers Automated Quotation System or by members of the National Association of Securities Dealers who maintain a market in such stock. The Assignor hereby grants to the Chief Executive Officer or Secretary of the Assignee an irrevocable special power of attorney, coupled with an interest, to take on behalf of the Assignor all actions necessary to transfer such Shares to such persons or entities as shall be entitled to acquire his Shares in accordance with the provisions of this Section 4(b).

5. Nonrecourse Debt. There shall be no personal liability to Assignor to pay the indebtedness evidenced by the Note, or for the performance of any of the terms, conditions or covenants expressed in the Note or this Collateral Assignment and Security Agreement; provided, however, in the event of default hereunder or under the Note, recourse shall be had only against the Collateral, and in any action or proceeding brought hereunder or on the Note, no deficiency or other money judgment shall be sought or obtained, and no cause of action shall lie against Assignor whether or not he or she is personally liable. It is further understood and agreed, however, that nothing contained in this paragraph shall in any manner or way affect or impair (i) the existence of the nonrecourse indebtedness evidenced by the Note; (ii) the enforceability of the lien and security interest created hereby; or (iii) the right to name Assignor as a defendant in any action instituted solely to foreclose the lien created hereby and divest Assignor of title to the Collateral.

6. No Implied Waiver. No waiver by the Assignee of any default shall operate as a waiver of any other default or of the same default on a future occasion. All rights of the Assignee hereunder will inure to the benefit of its respective successors and assigns and all promises and duties of the Assignor shall bind his heirs, executors, administrators, successors and assigns.

7. Governing Law. This Agreement shall be governed by and construed and interpreted in accordance with Texas law.

SIGNED as of the date first above written.

ASSIGNOR: (purchaser(s))

ASSIGNEE:

USR INDUSTRIES, INC.

By: _____
Chief Executive Officer

No person is authorized in connection with an offering made hereby to give any information or to make any representation other than as contained in this Prospectus and, if given or made, such information or representation must not be relied upon as having been authorized by the Company or by any underwriter. This Prospectus does not constitute an offer to sell or a solicitation of an offer to buy, by any person in any jurisdiction in which it is unlawful for such person to make such an offer or solicitation. Neither the delivery of this Prospectus nor any sale made hereunder shall under any circumstances create any implication that the information contained herein is correct as of any time subsequent to the date hereof.

400,000 Shares

Pinnacle Petroleum, Inc.

Common Stock

TABLE OF CONTENTS

	<u>Page</u>
Available Information	i
Incorporation of Certain Information by Reference	i
Information About Selling Stockholder	1
Risk Factors	1
The Offering	5
How to Subscribe	6
Use of Proceeds	10
Price Range of Pinnacle Common Stock	10
Business of Pinnacle	11
Description of Pinnacle Common Stock	16
Additional Information	16
Legal Opinion	16
Experts	16

PROSPECTUS
August 3, 1988

9

USR INDUSTRIES, INC.

Report to Stockholders

1987

XXIX-009

**Officers and Directors of
USR Industries, Inc.**

ANTHONY N. CIALONE

RALPH T. McELVENNY, JR.

✓ STEPHEN C. MILLER

JODY C. WELBORN

✓ CHARLES R. WHITE

Principal Occupation or Employment

President of AeroPanel Corporation

Chief Executive Officer of the Company;
Chairman of Pinnacle Petroleum, Inc.

Principal Accounting Officer
of the Company

Secretary of the Company

President of Isolite Corporation

Transfer Agent and Registrar

MOUNTAIN STATES TRANSFER AGENTS, INC.
DENVER, COLORADO

Special Counsel

HANNOCH WEISMAN
ROSELAND, NEW JERSEY

General Counsel

DAVIS GRAHAM & STUBBS
DENVER, COLORADO

Auditors

COOPERS & LYBRAND
HOUSTON, TEXAS

Corporate Headquarters

550 POST OAK BOULEVARD
SUITE 545
HOUSTON, TEXAS 77027

DEAR FELLOW STOCKHOLDERS:

USR Industries, Inc. (the "Company") is a diversified holding company with interests in the real estate and natural resources sectors. Despite areas of strength the Company's overall operations remain subject to significant contingencies beyond your management's control.

Litigation

The so-called "environmental" litigation remains the most significant contingency overhanging your Company. In that litigation claims are being asserted today which stem from events many years ago in the era of World War I. The allegations involve complex issues of law and speculation as to distant events. Indeed, most claims relate back to times before stockholders or members of the Company's management team were even born.

Unfortunately, our jury trial system provides strong financial incentives which encourage lawyers to assert grandiose claims. Such claims often use today's knowledge, recently enacted legislation or recent "judge made" law to attack practices which were widely accepted in earlier years. As a result, an inflammatory atmosphere has infected our tort law and created a national crisis in the insurance industry. Legislatures of several states have reformed their tort laws to restrict excessive claims. However, most states still allow lawyers who have huge personal financial stakes in their own cases to assert any amount of "damages" they desire. Your Company's experience reflects these dangerous trends.

Also during recent years, the precipitous declines of oil and gas prices have reduced the current value of your Company's ownership interest in the natural resources sector, the common stock of Pinnacle Petroleum, Inc.

Defense Agreement. Effective response to the environmental litigation was made possible by a Defense Agreement negotiated with five primary insurance companies. Under the Defense Agreement, which was executed in 1985, the insurers agreed to pay significant costs for defense of the litigation, while reserving the absolute right to deny liability on the underlying claims. However, substantial direct and indirect costs are not covered under the Defense Agreement, and these continue to burden your Company's financial and management resources.

No prediction can be made as to the final outcome of these complex legal matters. The Company's defense is dependent upon continued assistance from the insurers. An insurer's refusal to continue assistance—or a final judgment unfavorable to the Company—could lead to reorganization of your Company under the bankruptcy statutes. Your management is "cautiously optimistic" that the insurers will continue to provide assistance for the Company's defense. While the total amount of insurance coverage appears substantial, if any final judgment is entered against your Company on one of the underlying claims the insurance carriers may deny that their policies cover those claims. Further costly litigation might then be required to determine whether coverage is in place and, if so, in what amounts.

Real Estate Sector

During late 1987 your Company established an ownership interest in the real estate sector by purchasing a majority interest in a commercial office building in Houston, Texas. Purchase of the property, formerly owned by a German national, adds approximately \$3 million of real estate assets to your Company's consolidated balance sheet. To finance the purchase the Company formed a limited partnership and obtained additional funds through contributions and loans from the limited partners. A wholly owned real estate subsidiary of your Company serves as initial general partner of the partnership and manages the building on a standard fee basis. In recent years Houston real estate has received widespread negative publicity. However, the property—which is located in an attractive parklike setting on Houston's west side, and is over seventy percent leased—is felt to offer attractive potential for the future. Accordingly, the purchase meets the acquisition criteria previously established by management for the real estate sector.

Natural Resources Sector

Your Company holds an ownership interest in the natural resources sector through the common stock of Pinnacle Petroleum, Inc., an independent, publicly owned oil and gas exploration and production company. In the accompanying income statements, the Company's ownership of Pinnacle common stock

is accounted for under the equity method. Under the equity method the Company's income statement reflects its pro rata share of Pinnacle's operating results. In recent years virtually all independent oil and gas companies, including Pinnacle, have been adversely affected by the unprecedented declines in oil and gas prices. On the other hand, the industry downturn has provided opportunities to expand through acquisitions, mergers or other corporate transactions. Pinnacle's management has stated that Pinnacle is seeking additional corporate transactions.

Rights Offering. In order to strengthen liquidity and increase flexibility, the Company plans to offer stockholders the right to purchase a part of the Company's ownership position in Pinnacle common stock. Shares of Pinnacle common stock will be offered on a pro rata basis to all stockholders of the Company.

Asset Redeployment

Having completed its initial purchase in the real estate sector, your Company's program to redeploy assets out of small manufacturing and into the real estate and natural resources sectors is essentially complete. Active consideration is being given to the sale of the small remaining manufacturing line, which accounts for only approximately 3% of the Company's consolidated assets. Proceeds of such sale would be applied primarily to reduce indebtedness and to augment the Company's liquidity position.

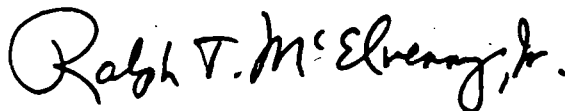
Management believes that the ownership interests in core sectors established under your Company's Plan of Asset Redeployment continue to offer attractive upside potential over the longer term. While the Company's ownership commitments are felt to have been well considered and carefully executed, of course neither the real estate nor natural resources sectors are immune from "macro" economic trends. For example, while real estate and natural resources are considered to offer a hedge against inflation, currently our domestic economy is not inflationary. The Company's strategic plan projects that Congress will continue to authorize government expenditures greatly in excess of income, and that in time a macro trend towards inflation will resume.

In Closing

Management remains deeply troubled by the withering litigation affecting USR Industries, Inc. On the other hand, your Company can look to several areas of relative strength which offer potential for the future.

On behalf of your Board of Directors I wish to extend thanks and appreciation to the many stockholders, talented outside professionals and friends of the Company for their efforts and support.

Respectfully submitted,



Ralph T. McElvenny, Jr.
Chief Executive Officer

April 22, 1988

USR INDUSTRIES, INC.
CONSOLIDATED BALANCE SHEETS

ASSETS	December 31, 1987	December 31, 1986
Current assets:		
Cash and equivalents	\$ 81,646	56,079
Accounts receivable:		
Trade	69,139	60,700
Pension termination	—	690,000
Other	21,185	4,543
Inventories	27,239	19,399
Note receivable-current portion	8,860	8,185
Common stock held for sale—Pinnacle Petroleum, Inc.	500,000	—
Prepaid expenses and other	5,999	3,556
Total current assets	<u>714,068</u>	<u>842,462</u>
Ownership of common stock—Pinnacle Petroleum, Inc.	1,138,234	2,139,086
Note receivable—Purchasing Corporations	474,762	461,627
Property, plant and equipment, at cost	4,610,576	1,688,390
Less accumulated depreciation	<u>(1,214,992)</u>	<u>(1,153,095)</u>
	<u>3,395,584</u>	<u>535,295</u>
Other assets	<u>111,547</u>	<u>88,868</u>
	<u><u>\$ 5,834,195</u></u>	<u><u>4,067,338</u></u>
 LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Notes payable and current maturities of long-term debt	\$ 216,055	230,000
Accounts payable	394,040	214,410
Accrued expenses	144,636	136,476
Total current liabilities	<u>754,731</u>	<u>580,886</u>
Other long-term liabilities	28,422	—
Deferred income	—	34,679
Long-term debt	2,005,957	—
Long-term obligation under capital lease	62,822	63,515
Minority interest—Partnership	369,123	—
Commitments and contingencies		
Stockholders' equity:		
Common stock, par value \$1; 3,500,000 shares authorized; issued and outstanding 994,655 shares at December 31, 1987 and 995,655 shares at December 31, 1986	994,655	995,655
Additional paid-in capital	365,461	366,011
Retained earnings	<u>1,253,024</u>	<u>2,026,592</u>
Total stockholders' equity	<u>2,613,140</u>	<u>3,388,258</u>
	<u><u>\$5,834,195</u></u>	<u><u>4,067,338</u></u>

See Notes to Consolidated Financial Statements

USR INDUSTRIES, INC.
CONSOLIDATED STATEMENTS OF OPERATIONS

	Years Ended December 31,		
	1987	1986	1985
Revenues:			
Net sales	\$ 367,446	337,631	246,411
Interest income	61,517	54,712	61,844
Rental income, net	82,827	67,500	10,642
Other income	61,505	30,488	39,929
Total revenues	<u>573,295</u>	<u>490,331</u>	<u>358,826</u>
Costs and expenses:			
Cost of sales	140,171	186,637	139,132
Selling, general and administrative expenses	579,822	462,417	342,710
Depreciation and amortization	81,561	86,510	99,755
Interest expense	46,823	23,891	40,025
Total costs and expenses	<u>848,377</u>	<u>759,455</u>	<u>621,622</u>
Gain (loss) on pension termination	10,323	690,000	—
Gain (loss) on sale of assets	5,000	(5,690)	—
Gain (loss) on sale of stock	—	—	(67,905)
Market value writedown of common stock— Pinnacle Petroleum, Inc.	(192,000)	—	—
Minority interest in net loss of Partnership	30,877	—	—
Equity in net earnings (loss) of Pinnacle Petroleum, Inc.	<u>(352,686)</u>	<u>(1,110,654)</u>	<u>(207,653)</u>
Earnings (loss) from continuing operations	<u>(773,568)</u>	<u>(695,468)</u>	<u>(538,354)</u>
Discontinued operations:			
Earnings (loss) from operations of discontinued businesses	—	—	(19,057)
Net earnings (loss)	<u>\$ (773,568)</u>	<u>(695,468)</u>	<u>(557,411)</u>
Earnings (loss) per share:			
Earnings (loss) from continuing operations	\$ (.78)	(.69)	(.52)
Earnings (loss) from discontinued operations	—	—	(.02)
Net earnings (loss)	<u>\$ (.78)</u>	<u>(.69)</u>	<u>(.54)</u>
Weighted average number of common shares and common share equivalents	<u>994,954</u>	<u>1,006,776</u>	<u>1,024,586</u>

See Notes to Consolidated Financial Statements

USR INDUSTRIES, INC.
CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY

	<u>Common Stock</u>		<u>Additional Paid-in Capital</u>	<u>Retained Earnings</u>	<u>Total Stockholders' Equity</u>
	<u>Shares</u>	<u>Amount</u>			
Balance at December 31, 1984	1,017,650	\$1,017,650	\$407,217	\$3,279,471	\$4,704,338
Net earnings (loss)	—	—	—	(557,411)	(557,411)
Issuance of common stock for exercise of option	30,000	30,000	48,600	—	78,600
Treasury stock acquisitions (par value method)	<u>(23,989)</u>	<u>(23,989)</u>	<u>(38,726)</u>	<u>—</u>	<u>(62,715)</u>
Balance at December 31, 1985	1,023,661	1,023,661	417,091	2,722,060	4,162,812
Net earnings (loss)	—	—	—	(695,468)	(695,468)
Treasury stock acquisitions (par value method)	<u>(28,006)</u>	<u>(28,006)</u>	<u>(51,080)</u>	<u>—</u>	<u>(79,086)</u>
Balance at December 31, 1986	995,655	995,655	366,011	2,026,592	3,388,258
Net earnings (loss)	—	—	—	(773,568)	(773,568)
Treasury stock acquisitions (par value method)	<u>(1,000)</u>	<u>(1,000)</u>	<u>(550)</u>	<u>—</u>	<u>(1,550)</u>
Balance at December 31, 1987	<u>994,655</u>	<u>\$ 994,655</u>	<u>\$365,461</u>	<u>\$1,253,024</u>	<u>\$2,613,140</u>

See Notes to Consolidated Financial Statements

USR INDUSTRIES, INC.
CONSOLIDATED STATEMENTS OF CHANGES IN FINANCIAL POSITION

	Years Ended December 31,		
	1987	1986	1985
SOURCES OF FUNDS:			
Earnings (loss) from continuing operations	\$ (773,568)	(695,468)	(538,354)
Items not affecting working capital:			
Depreciation and amortization	81,561	86,510	99,755
Accretion of discount on note receivable	(21,995)	(19,973)	(25,817)
(Increase) decrease in ownership of Pinnacle Petroleum, Inc.	(43,834)	—	14
(Gain) loss on sale of stock	—	—	67,905
(Gain) loss on sale of assets	(5,000)	5,690	—
Market value writedown of common stock	192,000	—	—
Minority interest in net loss of Partnership	(30,877)	—	—
Equity in net loss of Pinnacle Petroleum, Inc.	352,686	1,110,654	207,653
Funds provided by (used for) continuing operations	(249,027)	487,413	(188,844)
Earnings (loss) from discontinued operations	—	—	(19,057)
Funds provided by (used for) operations	(249,027)	487,413	(207,901)
Issuance of common stock for exercise of option	—	—	78,600
Limited partners capital contribution	400,000	—	—
Payments and current maturities of note receivable	8,860	38,785	12,853
Reclassification to common stock held for sale	500,000	—	—
Proceeds from sale of stock	—	—	300,000
Increase in notes payable	2,047,535	—	—
Increase in long-term lease obligations	—	63,515	—
Increase in deferred income	—	34,679	—
Increase in long-term liabilities	28,422	—	—
Proceeds from sale of assets	5,000	8,850	—
Net book value of non-current assets of discontinued operations	—	—	464,040
Decrease in other assets	—	49,756	30,326
Decrease in working capital	302,239	—	—
	<u>\$3,043,029</u>	<u>682,998</u>	<u>677,918</u>

See Notes to Consolidated Financial Statements

(Continued on next page)

USR INDUSTRIES, INC.
CONSOLIDATED STATEMENTS OF CHANGES IN FINANCIAL POSITION (Continued)

	Years Ended December 31,		
	1987	1986	1985
USES OF FUNDS:			
Additions to property, plant and equipment, net	\$2,941,850	96,790	1,643
Increase in other assets	22,679	—	—
Current maturities of long-term lease obligations	693	—	—
Payments and current maturities of notes payable	41,578	—	—
Increase in note receivable	—	—	467,475
Decrease in deferred income	34,679	—	—
Treasury stock acquired	1,550	79,086	62,715
Increase in working capital	—	507,122	146,085
	<u>\$3,043,029</u>	<u>682,998</u>	<u>677,918</u>
CHANGES IN COMPONENTS OF WORKING CAPITAL:			
Increase (decrease) in current assets:			
Cash and equivalents	\$ 25,567	35,923	(80,007)
Accounts receivable	(664,919)	301,277	28,589
Inventories	7,840	5,656	(268)
Note receivable	675	623	7,562
Common stock held for sale—Pinnacle Petroleum, Inc.	500,000	—	—
Prepaid expenses and other	2,443	(3,471)	(4,437)
Net assets of discontinued businesses held for sale	—	—	(403,435)
	<u>(128,394)</u>	<u>340,008</u>	<u>(451,996)</u>
Increase (decrease) in current liabilities:			
Notes payable and current maturities of long-term debt	(13,945)	—	(300,000)
Accounts payable	179,630	(156,944)	29,860
Accrued expenses	8,160	(10,170)	(327,941)
	<u>173,845</u>	<u>(167,114)</u>	<u>(598,081)</u>
Increase (decrease) in working capital	<u>\$ (302,239)</u>	<u>507,122</u>	<u>146,085</u>

See Notes to Consolidated Financial Statements

USR INDUSTRIES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(1) Summary of Significant Accounting Principles

Principles of Consolidation

The accompanying consolidated financial statements include the accounts of USR Industries, Inc. ("Industries") and its wholly owned subsidiaries Metal Fabricators, Inc., USR Lighting, Inc. ("Lighting"), USR Metals, Inc. ("Metals"), USR Chemicals, Inc., Unatco Funding Corporation, 550 POB, Inc. and Industries' majority owned limited partnership, Houston-Phoenix Co., Ltd. All significant intercompany accounts and transactions have been eliminated.

During 1985 in connection with various corporate transactions undertaken pursuant to its Plan for Corporate Development, Pinnacle Petroleum, Inc. ("Pinnacle") issued Convertible Voting Preferred Stock, Warrants and Common Stock. At December 31, 1985, after giving effect to the increased number of Pinnacle voting securities outstanding after such transactions, Industries' voting position was reduced to approximately 40% of Pinnacle's total voting securities then outstanding. At and subsequent to that time the consolidated financial statements of Industries present the ownership of common stock of Pinnacle under the equity method.

Inventories

Inventories of raw materials are carried at the lower of cost (first-in, first-out) or market. Work-in-process and finished goods inventories are valued at the lower of average cost or market.

Property, Plant and Equipment

Property, plant and equipment are depreciated over the estimated useful lives of the depreciable assets using the straight line method. Expenditures for maintenance and repairs which do not improve or extend the useful lives are charged to operations as incurred, while expenditures for major renewals and betterments are capitalized. Dispositions of assets are reflected at the historical costs less accumulated depreciation, with resulting gain or loss reflected in operations currently.

Federal Income Taxes

Industries and its wholly owned subsidiaries join in filing a consolidated federal income tax return. Investment tax credits are accounted for by the flow-through method.

Accruals and Reserves

The consolidated financial statements include a provision to the statement of operations established for the year ended December 31, 1983 for estimated future litigation expenses in connection with claims asserted against Industries and its wholly owned subsidiaries. The accrual of \$100,000 remains on the Consolidated Balance Sheets as of December 31, 1987 and 1986 with respect to such expenses. See Note 10.

Earnings Per Share

Net earnings (loss) per share of common stock are based on the weighted average number of shares of common stock and common stock equivalents from stock options. Exercise of

options outstanding at December 31, 1985 were calculated to have a dilutive effect and such options were included in the calculation of primary earnings per share using the treasury stock method. The effect of the exercise of such options on the fully diluted earnings per share was immaterial.

Financial Accounting Standards Board's ("FASB") Statement Release

The FASB issued a Statement of Financial Accounting Standards ("SFAS") No. 96 "Accounting for Income Taxes" in December 1987. The SFAS requires substantial changes in the method of accounting for deferred income taxes and must be adopted by Industries beginning in 1989. Industries has no deferred taxes recorded and is currently in a net operating loss carryforward position. Industries has not yet adopted SFAS No. 96 and, accordingly, the impact on Industries' financial condition and results of operations has not been determined; however, Industries does not expect its adoption to have a material adverse effect.

Reclassifications

Presentation of the financial statements for 1986 has been changed to conform with the 1987 financial statement classifications. Such reclassifications have no effect on results of operations as reported previously.

(2) Ownership of Securities of Pinnacle Petroleum, Inc.

On June 20, 1985, Industries sold 111,111 shares of Pinnacle Common Stock to Pinnacle for a net price of \$2.70 per share. Industries, which purchased such shares from Pinnacle in December 1983, realized a loss of \$67,905 on the sale after giving effect to basis adjustments since the purchase date. On the date of sale, Pinnacle Common Stock was reported in the over-the-counter market at \$1.50 bid and \$1.75 asked per share. The Chairman of Industries also serves as Chairman of Pinnacle. Also during 1985, Pinnacle issued Convertible Voting Preferred Stock, Warrants and Common Stock in connection with acquisitions. After giving effect to the increased number of shares of Common and Preferred Stock issued in connection with such transactions, at December 31, 1985 Industries' voting position was reduced to approximately 40% of Pinnacle's total voting securities then outstanding and is accounted for under the equity method.

At Pinnacle's 1986 Annual Meeting, stockholders approved a Class B Proposal (the "Proposal") pursuant to which stockholders could elect on a "one-time only" basis to exchange shares of Pinnacle Common Stock, on which a Warrant Dividend had been declared under the Proposal, for shares of Class B Common Stock on a share-for-share exchange. The Class B Common Stock has the right to elect a majority of Pinnacle's Board of Directors and certain other greater voting rights, but was not eligible to receive the Warrant Dividend and is not freely tradeable. So as to receive the Warrant Dividend, which was distributable only to holders of the fully marketable

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

Common Stock, Industries elected to continue to hold its shares of Common Stock. Upon distribution of the Warrant Dividend, Industries received a total of 205,759 Warrants from Pinnacle, with each Warrant entitling the holder to purchase one share of Common Stock of Pinnacle, subject to postponement in certain events. Subject to certain conditions Warrants are exercisable from April 1, 1988 until May 31, 1988 and from April 1, 1989 until May 31, 1989 at exercise prices of \$1.35 per share and \$1.50 per share, respectively. However, the Board of Directors of Industries has been advised that the initial exercise date will be postponed for 180 days as provided by the terms of the Warrant. Industries' ownership position in Pinnacle Common Stock represented approximately 44% of the total number of shares of Pinnacle Common Stock outstanding at December 31, 1987. During 1987 Industries received an additional 29,223 shares of Pinnacle Common stock as a result of terminating its pension plans as further discussed in Note 5. Such shares are included in Industries' ownership of Pinnacle Common Stock above.

Industries anticipates during 1988 certain shares of Pinnacle Common Stock will be offered to its stockholders through a rights offering. Industries recorded a writedown of the book value of such shares of \$192,000 for 1987 and the adjusted amount was reclassified as a current asset at December 31, 1987.

Summarized financial information for Pinnacle is shown below. Additional information concerning Pinnacle is contained in Pinnacle's own periodic filings and Annual Reports on Form 10-K.

	December 31,	
	1987	1986
Current assets	\$3,513,141	4,494,277
Property and equipment, net	2,354,516	2,394,146
Other assets	78,820	—
	<u>\$5,946,477</u>	<u>6,888,423</u>
Current liabilities	\$ 697,118	572,994
Convertible preferred stock—redeemable	—	450,000
Minority interest—Regal Petroleum, Ltd.	1,357,049	1,560,999
Stockholders' equity	3,892,310	4,304,430
	<u>\$5,946,477</u>	<u>\$6,888,423</u>

	Years Ended December 31,		
	1987	1986	1985
Revenues	\$1,029,108	1,034,091	672,318
Costs and expenses	2,019,019	4,058,364	1,003,405
Earnings (loss) from operations	(989,911)	(3,024,273)	(331,087)
Minority interest in net loss of Regal Petroleum, Ltd.	203,950	923,560	—
Equity in net loss of Regal Petroleum, Ltd.	—	—	(16,166)
Net earnings (loss)	<u>\$ (785,961)</u>	<u>(2,100,713)</u>	<u>(347,253)</u>

(3) Discontinued Operations

Effective February 13, 1985 certain net assets of Lighting and Metals were sold to newly formed corporations owned by the Chairman of Industries (the "Purchasing Corporations"). In connection with its review of the transaction, the Board of Directors of Industries received the written opinion of an independent financial institution that the transaction would be fair, from a financial point of view, to Industries and its stockholders. At a Meeting held March 7, 1986 Industries' stockholders approved and ratified the sales transactions.

As consideration for the net assets sold, Lighting and Metals received proceeds having a total face amount of \$1,064,000 of which \$400,000 was paid in cash at closing with the balance paid in installment notes issued by the Purchasing Corporations having an aggregate face value of \$664,000. For financial statement reporting purposes, the principal amount of such notes receivable of \$664,000 was discounted as of February 13, 1985, their date of issue, to an assumed market interest rate of 11% resulting in a discount of \$196,525 from the original face value of the notes to an adjusted principal amount of \$467,475. The terms of the notes call for principal and interest payments to be received in varying installments through March 31, 1995.

During 1987, 1986 and 1985 interest income from the notes of the Purchasing Corporations totalled \$55,045, \$53,646 and \$59,893 of which \$21,995, \$19,973 and \$25,817, respectively, were attributable to accretion of the original issue discount discussed above.

In connection with such transactions, the landlord of a small office facility leased on a long term basis by Lighting refused consent to assignment of such lease to one of the Purchasing Corporations. During May 1986 Lighting instituted legal action in New Jersey Superior Court seeking a judicial determination as to the status of the lease. The landlord answered with denials and counterclaims and instituted separate legal action in Federal District Court which has been stayed pending the outcome of the state court action. Thereupon motion for summary judgment against the landlord was made in Superior Court by Lighting and Industries. On December 19, 1986 the Superior Court granted that motion for summary judgment. In granting summary relief to Lighting and Industries, the Superior Court held that the lease had not been assigned as a matter of law, and remained in effect.

The landlord took an appeal to the Appellate Division from the Superior Court decision. During late 1987 the Appellate Division unanimously affirmed the action of the Superior Court in granting summary judgment in favor of Lighting and Industries.

The landlord then petitioned the Supreme Court of the State of New Jersey for review of the unanimous Appellate Division ruling against the landlord. By order dated March 10, 1988 the Supreme Court denied the landlord's petition. (See Note 10 and 10(g).)

During 1986 Lighting, Industries and the Purchasing Corporation mutually agreed to exclude any transfer of such lease

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

from the transactions. Accordingly, for the year ended December 31, 1986 and thereafter the long-term obligations and related sublease income attributable to such lease continue to be presented on the consolidated financial statements of Industries.

The asset sales transactions are subject to certain conditions subsequent, including the right of the Purchasing Corporations to rescind the transactions and to be repaid the purchase price in full in the event that their counsel shall, prior to December 31, 1988, advise that there is any question whether the assets were purchased "free and clear" of claims against Industries or its subsidiaries. Such date may be further extended by mutual agreement of the parties.

(4) Property, Plant and Equipment

A summary of property, plant and equipment at December 31, 1987 and 1986 is as follows:

	December 31,	
	1987	1986
Buildings	\$ 3,120,766	183,254
Machinery and equipment	860,016	875,342
Office furniture and fixtures	70,148	70,148
Leasehold improvements	559,646	559,646
	4,610,576	1,688,390
Less accumulated depreciation	(1,214,992)	(1,153,095)
	<u>\$ 3,395,584</u>	<u>535,295</u>

(5) Pension Plans

In 1985 and 1986, Industries and its wholly owned subsidiaries had two pension plans which covered substantially all hourly and salaried employees. Industries made annual contributions to the plans equal to the amounts accrued for pension expense and based on actuarial determination. Pension expense included amortization of past service costs over a maximum of 40 years. During 1985 and 1986 Industries incurred no pension expense as the plans were fully funded.

Effective December 31, 1986 the foregoing defined benefit pension plans were terminated. In connection with the termination, Industries recorded a receivable of \$690,000 in its consolidated financial statements at December 31, 1986 to reflect the estimated recovery of assets in excess of the accumulated plan benefits and costs associated with plan terminations. During the third quarter of 1987 such receivable was collected in full.

Effective January 1, 1987, Industries adopted a 401(k) savings plan. The plan covers all employees who have completed one or more years of service and are not covered by a collective bargaining agreement. Each participant may make annual contributions up to the lesser of \$7,000 or 13% of compensation. Industries, at its discretion, may match a participant's contribution up to 2% of compensation. Participant contributions are vested at all times, and the discretionary employer contributions vest 20% per year after two years. Industries incurred no contribution expense in 1987. Additionally, effective January 1, 1987 Industries adopted a defined benefit plan for all employees covered by a collective bargaining agreement. Industries' annual

contribution to the plan is actuarially determined. Participants in the plan are fully vested after five years of service. The actuarial status of the defined benefit plan at December 31, 1987 has not been determined; however, management does not consider the impact of the plan to be material to the consolidated financial statements.

(6) Federal Income Taxes

For federal income tax purposes at December 31, 1987 Industries and its wholly owned subsidiaries had net operating loss carryforwards of approximately \$436,000 which expire at various dates through the year 2002 and investment tax credit carryforwards of approximately \$28,700 which expire through the year 2000.

For financial reporting purposes at December 31, 1987 Industries and its wholly owned subsidiaries had \$2,729,000 of net operating loss carryforwards and approximately \$5,600 of investment tax credit carryforwards. Certain items of income and expense, primarily depreciation, are recognized for income tax purposes in amounts and periods which differ from those recognized for financial reporting purposes. Investment tax credit carryovers have been reduced in accordance with the Tax Reform Act of 1986.

(7) Common Stock

At a Meeting held on June 13, 1984 stockholders of Industries adopted an Employees' Incentive Stock Option Plan covering 50,000 shares of Common Stock. On December 27, 1984 the Board of Directors approved the grant of an option to an officer of Industries covering 30,000 of such shares exercisable at any time in whole or in part through December 26, 1989 at a price of \$2.62 per share. The exercise price was equivalent to 110% of the closing price of Industries' Common Stock on the American Stock Exchange as of the date of grant. During 1985 that officer exercised such option in full and paid to Industries a total of \$78,600.

Where its overall business objectives and current liquidity position permit, Industries may purchase its Common Stock in open market or private transactions from time to time. Subject to the availability of funds, market conditions and other factors Industries may make purchases in the future. Treasury stock is recorded on the par value method.

(8) Leases

Industries' principal offices are located at 1717 Woodstead Court, Suite 113, The Woodlands, Texas 77380. The offices consist of approximately 2,000 square feet leased from an unaffiliated party on a month-to-month basis. During April 1988 Industries will move its offices to the office building in which Industries has acquired a substantial ownership interest, further described at Note 11. That building is located at 550 Post Oak Boulevard, Houston, Texas 77027, and has approximately 53,700 net rentable square feet. Industries had leased approximately 2,000 square feet of office space on a three-year lease through December 31, 1990.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

Industries' wholly owned subsidiary, Lighting, leases an office building and a manufacturing facility under long-term capital and operating leases, respectively. The leases contain varying terms and renewal options. Both facilities leased by Lighting are subleased at rentals in excess of their lease expense. Industries did not itself guarantee any obligation under the operating lease.

At December 31, 1987, the aggregate future minimum lease payments under the capital lease and Lighting's noncancellable operating lease are as follows:

	<u>Capital Lease</u>	<u>Operating Lease</u>
1988	\$ 5,318	\$127,000
1989	5,318	127,000
1990	5,318	127,000
1991	5,318	127,000
1992	5,318	127,000
Subsequent to 1992	<u>130,303</u>	
Total minimum lease payments	156,893	
Less amount representing interest	<u>(93,378)</u>	
Present value of future minimum lease payments	63,515	
Less current obligation	<u>(693)</u>	
	<u>\$ 62,822</u>	

Total rental expense on the operating lease was approximately \$127,000 for each of the years ended December 31, 1987, 1986 and 1985. Sublease rental income under the operating lease for the years ended December 31, 1987, 1986 and 1985 was approximately \$166,000, \$194,000 and \$111,000, respectively from the Purchasing Corporations. Future sublease rental income under current sublease contracts respecting the operating and capital leases is scheduled to be approximately \$662,000. For financial reporting purposes, sublease rental income is recorded net of rental expense.

In connection with its acquisition of the office building, Houston-Phoenix Co., Ltd., the limited partnership which purchased the building (the "Partnership"), has leased office space to tenants under various operating leases. At December 31, 1987 future minimum lease payments to be received from such operating leases are as follows:

<u>Year Ended December 31,</u>	
1988	\$ 407,353
1989	424,098
1990	366,729
1991	142,441
1992	5,639
	<u>\$1,346,260</u>

Options for renewals exist ranging in terms from three to five years and in rates from \$13.00 per square foot to 95% of the prevailing base rental for like space but not less than \$10.50 per square foot.

(9) Notes Payable and Long-term Debt

Notes payable and long-term debt at December 31, 1987 consisted of the following:

	<u>December 31, 1987</u>
Commercial bank note	\$ 180,000
Mortgage note	1,942,012
Notes to limited partners	<u>100,000</u>
	2,222,012
Less current maturities	<u>(216,055)</u>
	<u>\$2,005,957</u>

The commercial bank loan, which is collateralized by shares of Common Stock of Pinnacle, bears interest at the rate of prime plus 2% (8.75% at December 31, 1987) and matures on September 30, 1988. The mortgage note payable bears an interest rate of 9.625% and is collateralized by the office building. The mortgage note is due in monthly installments of \$18,371 which include principal and interest with the balance of \$1,502,683 due in August 1996. The notes to limited partners bear interest at 8% per annum with interest due annually and principal due at the earlier of December 31, 1997 or the substantial disposition of the assets of the Partnership. These notes are collateralized by the general partners' interest in the Partnership. Scheduled maturities at December 31, 1987 for each of the five years through December 31, 1992 are \$216,055, \$38,582, \$42,463, \$46,736 and \$51,438, respectively.

(10) Commitments and Contingencies

Legal Proceedings

(a) On April 2, 1981 an action was commenced in the Superior Court of New Jersey, Essex County, by T & E Industries, Inc. naming United States Radium Corporation ("USRC"), the corporate predecessor to Safety Light Corporation ("SLC"), as a defendant and alleging, inter alia, that property in Orange, New Jersey owned by the plaintiff suffers from contamination from certain radioactive materials allegedly deposited thereon by USRC during prior years. The litigation arises from operations conducted by USRC at the site during the years 1917 to 1926. Subsequent to the commencement of this action the complaint was amended to include Industries and certain of its subsidiaries alleged to be corporate successors to the former USRC. The plaintiff seeks to compel remedial action as to alleged improper condition of the site and damages in unspecified amounts in compensation for injury to its property and business as well as punitive damages.

During December 1983 plaintiffs amended such complaint to include as additional defendants GAF Corporation, Mitsubishi Chemical Industries, Inc. ("MCI") and MCI's subsidiary in New Jersey, USR Optonix, Inc., which was alleged to be a corporate successor to the former USRC. The additional defendants were claimed to be liable under the product line exception to the general theory that a third party purchaser of assets is not liable as a successor. The additional defendants answered denying liability and demanded that the previously

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

named defendants defend the action on their behalf and indemnify them against costs and any potential liability in connection therewith. In 1984 the additional defendants were successful on a motion for summary judgment against the plaintiffs and, accordingly, the claims of the additional defendants against Industries and its subsidiaries have been dismissed.

In early 1985 Industries prevailed against a motion for summary judgment by the plaintiff seeking judgment that Industries is the successor to USRC.

In September 1985 five primary insurance carriers of Industries and SLC assumed the defense of Industries, certain of Industries' subsidiaries and SLC, pursuant to a Defense Agreement. While the insurance carriers are assisting in the defense of certain actions their defense is made subject to an absolute reservation of rights to deny liability on any of the underlying claims.

On February 3, 1986, this matter was tried to a jury before the Honorable Stanley G. Bedford. This trial was only with respect to the liability, if any, of SLC. Prior to trial, the Court bifurcated the count asserting liability against Industries and certain of Industries' subsidiaries and on November 18, 1985 ordered that all claims against Industries would be severed and separately tried, if at all, in the event plaintiff obtains a judgment against SLC.

During trial the Court granted a directed verdict in favor of SLC dismissing all of plaintiff's strict liability claims, all negligence based claims relating to the conduct of USRC between 1917-1926, and all claims based upon fraud, recklessness and intentional conduct. The only remaining claims against SLC were an alleged negligent failure to warn when the premises were sold in 1943 and a negligence theory which allegedly placed upon USRC a continuing duty to warn prospective purchasers up through the time plaintiff purchased the property in 1974, thirty-one years later. The Court also reduced plaintiff's damage claim from \$2.8 million to under \$400,000.

On March 11, 1986, the jury returned a verdict, finding that USRC was not negligent in 1943 when it failed to warn its immediate purchaser that the presence of radioactive tailings on the premises constituted a potential risk to health or property. The jury did find that USRC was negligent for not warning plaintiff before its purchase of the property thirty-one years later, in 1974, that the same potential risk to health or property existed on the premises. Damages were assessed against SLC in the amount of \$372,100.62.

On April 25, 1986, Judge Bedford granted SLC's motion for judgment in its favor notwithstanding the jury's verdict of March 11, 1986. The Court also denied plaintiff's application for indemnification by SLC of all cleanup costs assessed against plaintiff as a result of any future government efforts to decontaminate the property. Final judgment was thereafter entered in favor of SLC, Industries and certain of Industries' subsidiaries on May 29, 1986 and awarded on June 20, 1986, dismissing all of plaintiff's claims in their entirety.

On July 9, 1986, plaintiff filed a Notice of Appeal from the June 20, 1986 judgment. On February 24, 1988 oral argument on plaintiff's appeal was heard by the Appellate Division of the State of New Jersey. No prediction can be made concerning the outcome of such argument on appeal or when the three-judge panel of the Appellate Division may render its decision.

Since plaintiff's claims against Industries and certain of Industries' subsidiary companies will only be litigated in the event plaintiff is ultimately successful in its appeal against SLC, it is unclear at this time when, if at all, such claims will be tried. If a trial against Industries and certain of its subsidiaries does occur there remains to be resolved the outstanding issues of indemnification by SLC and crossclaims between it and Industries.

Claims also were made by T & E Industries in an action brought in the U.S. District Court for the District of New Jersey, allegedly pursuant to the Comprehensive Environmental Response, Compensation Liability Act of 1980 ("CERCLA") seeking a declaration that defendants are liable for all costs of cleanup and decontamination, consistent with the National Contingency Plan, of the site presently known as 422 Alden Street, Orange, New Jersey and seeking a judgment for "response costs" already incurred and injunctive relief for enforcing such remedy. Defendants made a motion to dismiss and plaintiffs made a cross-motion for partial summary judgment against SLC. The motions were heard on February 10, 1988. The Court, through Judge Wolin, found against the defendants' motion to dismiss based on New Jersey's "entire controversy doctrine" and granted T & E's application that SLC is liable under CERCLA for all necessary costs of response incurred by T & E which are consistent with the National Contingency Plan. The Court, however, limited T & E's alleged damages and determined, inter alia, that T & E's claim for attorney's fees are not recoverable response costs under CERCLA. Defendants are considering filing a petition with the Federal District Court to have the issue involving the entire controversy doctrine certified to the United States Court of Appeals for the Third Circuit. No such petition has been filed to date.

At this time, neither counsel nor management can predict the outcome of the litigation.

(b) On December 6, 1982 an action was commenced in the Superior Court of New Jersey, Essex County, by Leslie Zwain et al. naming as defendants SLC, Industries and certain of Industries' subsidiaries alleged to be corporate successors to the former USRC and claiming, inter alia, that because of alleged contamination of the site in Orange, New Jersey, described in (a) above, the plaintiffs have suffered business interruption, diminution of property values, mental anguish and loss of consortium. The plaintiffs seek compensatory and punitive damages in amounts to be established at trial.

On August 5, 1985, the Court dismissed plaintiffs' personal injury claims based upon plaintiffs' failure to institute legal action within the applicable statute of limitations period. On February 25, 1986 the Appellate Court reversed this dismissal

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

and remanded the matter for further proceedings. Defendants' application for leave to appeal this issue to the New Jersey Supreme Court was subsequently denied.

On November 30, 1987 the foregoing action was settled.

As in the T & E Industries litigation, the same five primary insurance carriers of Industries and SLC have assumed the defense of Industries, certain of Industries' subsidiaries and SLC, with a complete reservation of their rights to deny liability on the underlying claims.

(c) During 1984 and 1985 SLC, Industries and its two manufacturing subsidiaries, USR Lighting, Inc. and USR Metals, Inc., were named as defendants in five actions commenced in Superior Court, Essex County, New Jersey. These actions were brought on behalf of certain residents in the Townships of Montclair, Glen Ridge and West Orange, New Jersey and claim, inter alia, damages to land and personal injury in amounts to be proved at trial as well as punitive damages. Such alleged damages are claimed to have been caused by actual or threatened exposure of the property and persons of plaintiffs to levels of radon gas, a radioactive decay product of uranium or radium bearing ores, at levels above background levels naturally occurring and in excess of permissible levels established by the government for members of the public. Plaintiffs allege that such radon gas is a product of landfill obtained from the former USRC site in Orange, New Jersey.

By notice of motion returnable on July 18, 1986, Industries, certain of Industries' subsidiaries and SLC moved for summary judgment dismissing plaintiffs' claims based upon the continued lack of a factual nexus between their activities and the presence of radon in plaintiffs' homes. The motion was also based upon the inapplicability of the legal theories advanced by plaintiffs to these matters. By order dated August 22, 1986, the Court granted in part and denied in part the motion for summary judgment, ruling that there remained factual issues preventing the dismissal of certain claims which could not be resolved without a full plenary hearing. The Court dismissed all causes of action based upon manufacture of a defective product, breach of an express or implied warranty, battery and trespass. By the same order, the Court also consolidated these matters for discovery and trial purposes.

By order dated January 16, 1987, the Court granted the motion filed by Industries, certain of Industries' subsidiaries and SLC for severance and separate trial of certain liability and damage issues. The Court directed that these matters be tried in three separate phases: (1) a Phase I trial relating solely to plaintiffs' claims that the allegedly contaminated soil around plaintiffs' homes originated at the former USRC site in Orange, New Jersey; (2) if plaintiffs are successful in the Phase I trial, a second trial would follow encompassing all remaining liability issues; and (3) if plaintiffs are successful again in the Phase II trial, a third trial would follow relating to plaintiffs' personal injury and property damage claims.

On November 19 and 20, 1987 the defendants' motion for partial summary judgment regarding the absence of contaminated soil originating from the Orange site of the former USRC on plaintiffs' property was argued before the Superior Court of New Jersey, Law Division, Essex County. By letter opinion dated January 28, 1988, as supplemented February 4, 1988, the Court granted-in-part and denied-in-part defendants' application. The Court adjudicated as a fact that there is no contaminated fill originating from the Orange site on six of the properties claiming to be contaminated and directed a hearing, with further expert testimony, regarding the alleged presence of contaminated subsurface material on 14 properties as well as 30 remaining properties where certain bore hole sampling results were relied upon. On March 18, 1988, the Court denied plaintiffs' request for a rehearing on defendants' motion, as well as plaintiffs' request for leave to perform additional bore hole sampling and analysis to oppose defendants' application. The Court directed that within 90 days, plaintiffs are to provide defendants with a report from each expert plaintiffs intend to produce at the aforesaid hearing. Defendants will have 30 days from the receipt of same to submit a report from each expert, if any, defendants intend to produce at the hearing. A date for that hearing has not yet been set by the Court.

Based upon the current state of the law and the absence of evidence indicating that the activities of Industries or its subsidiaries are in any way related to the alleged presence of radon in and around plaintiffs' homes, there exist numerous defenses going to the merits in these actions.

As in the T & E Industries and Zwain matters, the same five primary insurance carriers of Industries and SLC have assumed the defense of Industries, certain of Industries' subsidiaries and SLC, with a complete reservation of rights.

At this time neither counsel nor management can predict the outcome of the litigation.

(d) On May 15, 1986, an action was commenced in the Superior Court of New Jersey, Essex County, by the Estate of Alexander F. Masson, et al. naming as defendants SLC, Industries and its two former manufacturing subsidiaries, USR Lighting, Inc. and USR Metals, Inc. This action is brought on behalf of the estate of a deceased resident of the Township of Montclair and the deceased plaintiff's brother who allege that the defendants are responsible for the presence of radon gas which was discovered in and around the deceased plaintiff's home. As with the actions identified in (c) above, plaintiffs allege that such radon gas is a product of landfill obtained from the former USRC site in Orange, New Jersey. Plaintiffs allege that the radon gas was the contributing and/or sole cause of the deceased plaintiff contracting lung cancer. Plaintiffs have also named four tobacco companies alleging that cigarettes manufactured by those defendants and smoked by the deceased plaintiff were also the contributing and/or sole cause of the deceased plaintiff contracting cancer.

Based upon the current state of the law and the absence of evidence indicating that the activities of Industries or its subsidiaries are in any way related to the alleged presence of radon

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

in and around plaintiff's homes, there exists numerous defenses going to the merits of this action.

As in the matters identified in (a), (b) and (c) above, the same five primary insurance carriers of Industries and SLC have assumed the defense of Industries, certain of Industries' subsidiaries and SLC, with a complete reservation of rights.

At this time neither counsel nor management can predict the outcome of the litigation.

(e) U.S. Environmental Protection Agency Proceedings

The U.S. Environmental Protection Agency ("EPA") has included the Orange, New Jersey site and the Montclair, Glen Ridge and West Orange sites on the national priorities list of the Comprehensive Environmental Response Compensation Liability Act of 1980, 42 U.S.C. 9601, and has notified Industries that it may be a potentially responsible party under that Act. Industries has provided requested information to the EPA. In view of the decision of Judge Wolin of the U.S. District Court declaring SLC a liable party under CERCLA for the remediation and cleanup for the Orange site the defendants are contacting the EPA to inquire whether the defendants participation in the remediation study of the Orange site being conducted by the EPA is a feasible alternative. Currently the defendants are informed that the EPA has contracted with an engineering firm regularly used by the EPA for that purpose to prepare and deliver a revised remedial investigation and study for the Orange site.

In late 1984, one of Industries' primary insurance carriers assumed the defense of Industries and certain of its subsidiaries in this potential lawsuit, while reserving its rights to disclaim liability.

(f) Proceedings Against Certain Insurers

During 1984 Industries notified its insurance carriers as to the pendency of certain of the above described actions and requested that such carriers defend and indemnify Industries as a named insured under various primary insurance policies as well as excess coverage or umbrella policies. All such carriers answered denying liability and denying any obligation to defend Industries against the claims asserted. Thereupon on August 20, 1984 Industries commenced an action in Superior Court of New Jersey, Essex County, naming as defendants all of Industries primary and excess coverage insurers and seeking judicial determination as to such carriers' duty to defend and to indemnify Industries and its subsidiaries and seeking reimbursement of costs expended by Industries for its defense, assumption of such defense on an ongoing basis, damages for wrongful declination to defend and punitive damages and counsel fees for willful failure to defend and indemnify Industries in each of the foregoing actions.

In September 1985, five primary insurance carriers of Industries and SLC assumed the defense of Industries and certain of its subsidiaries alleged to be successors in certain of the underlying actions described above, while reserving their right to disclaim liability. As a result of that Agreement, this action has been stayed except with respect to applications by plaintiffs

to require other primary insurance carriers not party to the Defense Agreement to provide for a defense indemnification of Industries, certain of Industries' subsidiaries and SLC.

While there can of course be no assurance as to the outcome of this action Industries has been advised that it has meritorious claims to support its actions for defense and indemnification.

Because of the uncertainties associated with the litigation described in (a) through (e) above, the liability of Industries and its subsidiaries alleged to be corporate successors to the former USRC cannot reasonably be estimated at this time, nor can an estimate of any ultimate liability or any insurance proceeds be made with any degree of certainty. Therefore, no such liability has been recorded in the financial statements.

(g) Blanchard Litigation

(i) Following several years of disputes and litigation involving one William C. Blanchard, a principal in an entity styled as Blanchard Securities Co. and the owner of 100 shares of Common Stock of Industries (together herein "Blanchard"), on May 22, 1986 Industries filed a lawsuit in New Jersey Superior Court, Law Division, naming Blanchard as a defendant. The action sought judicial declaration as to the status of a lease covering a small office premises in Morristown, New Jersey owned by Blanchard and subject to a long term lease entered into by Blanchard in 1955 (the "1955 Lease").

The 1955 Lease was one of several long term "credit leases" entered by Blanchard in order to utilize the credit of long term tenants to obtain construction financing for itself. As such the 1955 Lease provides for an initial term of 20 years through 1975 with four optional renewals of ten years each through 2015. After repeated demands by Industries' counsel, during 1980 Blanchard consented in writing to the sublease of the subject premises and, after further demands, during 1982 Blanchard consented to assignment of the 1955 Lease to Lighting.

In connection with the sale of the business and net assets of Lighting effective February 13, 1985 it was anticipated that the 1955 Lease would be assigned to the Purchasing Corporation. However, when Blanchard's consent to that assignment was requested, Blanchard claimed the 1955 Lease had been violated by an "unauthorized assignment" allegedly completed without Blanchard's approval and advised that Blanchard considered the 1955 Lease "terminated" and that Blanchard considered itself entitled to reenter and assume control over the premises.

In answering the litigation filed against it in Superior Court, Blanchard denied Industries' claims and interposed counter-claims alleging, inter alia, that an unauthorized assignment of the 1955 Lease had occurred and that such assignment was fraudulent, in violation of Blanchard's rights as a shareholder of Industries, in violation of fiduciary duties, securities laws, the Racketeer Influenced and Corrupt Organization Act and other related claims. Industries denied Blanchard's claims and thereupon filed a motion for summary judgment against Blanchard on one count.

On December 19, 1986 the Superior Court granted Industries' motion for summary judgment. In granting summary relief

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

to Industries the Court held that the 1955 Lease had not been assigned as a matter of law, and remained in effect.

Blanchard took an appeal from the Superior Court decision. During late 1987 the Appellate Division affirmed the action of the Superior Court in granting summary judgment in favor of Industries. The opinion of the Appellate Division was unanimous.

Blanchard then petitioned the Supreme Court of the State of New Jersey seeking review by the Supreme Court of the unanimous Appellate Division ruling against Blanchard. By order dated March 10, 1988 the Supreme Court denied Blanchard's petition.

(ii) In a separate action by Blanchard in U.S. District Court for the District of New Jersey, Blanchard repeated the claims asserted in the Superior Court action discussed above, alleging fraud, breach of fiduciary duties, violations of the Racketeer Influenced and Corrupt Organization Act, securities fraud and related claims, and named as defendants Industries, Lighting, the Purchasing Corporation and certain directors of Industries. Industries and other defendants in this action have moved to dismiss Blanchard's claims but the action has been stayed pending the outcome of the litigation begun in New Jersey Superior Court.

Industries believes that the Federal Court will give preclusive effect to the New Jersey state court judgments and that the likelihood of any material recovery against the defendants is remote.

(11) Acquisition of Certain Realty Assets

On November 20, 1987 Industries acquired a majority interest in a commercial office building located at 550 Post Oak Boulevard, Houston, Texas 77027. The purchase was made through a Texas limited partnership, Houston-Phoenix Co., Ltd. A wholly owned subsidiary of Industries, 550 POB, Inc. (the "Subsidiary") serves as the general partner of the Partnership and manages the property.

The building has a total of approximately 53,700 rental square feet and is approximately 75% leased, including leases with Industries, Pinnacle and Regal Petroleum, Ltd. ("Regal"), a majority owned subsidiary of Pinnacle, which will locate their offices in the building. Industries has entered into a three-year lease for approximately 2,000 rentable square feet at an initial annual rental rate of approximately \$10.00 per square foot through December 31, 1990, and Pinnacle and Regal have each entered leases having similar terms and rentals and covering approximately 1,500 rentable square feet.

To obtain the necessary financing to make the purchase Industries requested additional participation from an unaffiliated person and an officer and director of Industries, who put up the necessary additional financing through the purchase of limited partnership interests. The Partnership acquired the building from an unaffiliated third party for a total purchase price of approximately \$2,937,512. The purchase was financed through capital contributions to the Partnership totaling

\$900,000 of which \$500,000 was contributed by the Subsidiary and \$400,000 through the sale of the limited partnership interests. Such interests were purchased for the same pro rata price as was paid by Industries. In addition, the limited partners made loans to the Partnership in total amount of \$100,000 and the Partnership assumed a mortgage on the property in principal amount of approximately \$1,950,000. The loans from the limited partners bear interest at 8% per annum, with the Partnership obligated to pay interest only until maturity at the earlier of December 31, 1997 or the sale of all or substantially all of the Partnership's assets. The limited partners can not be required to make any additional capital contributions to the Partnership.

In connection with the purchase transaction, the Board of Directors of Industries received the written opinion of an independent mortgage banking firm which services in excess of \$1 billion of mortgages in the Houston area to the effect that the lease terms negotiated by the Partnership with affiliated tenants, including Industries and Pinnacle, are fair and fall within prevailing market rates for the Houston area.

The Subsidiary and the limited partners will participate in Partnership profits and distributions in proportion to their relative net capital contributions. The interest of the limited partners in the Partnership, other than any limited partnership interest which may later be acquired by the Subsidiary or the Partnership, is represented by Class A Units. For tax purposes, any Partnership losses or tax credits will be allocated one percent to the Subsidiary and ninety-nine percent to the limited partners. In addition to its participation in profits, losses and distributions of the Partnership, the Subsidiary manages the property for which the Subsidiary will be paid a management fee comparable to that generally charged for similar services in the Houston area, in no event to exceed five percent of gross revenues. In addition, the Subsidiary is reimbursed for all direct expenses incurred on behalf of the Partnership and for its general and administrative expenses allocable to Partnership operations.

Under the limited partnership agreement, the Partnership has agreed to indemnify the Subsidiary and the limited partners against certain liabilities relating to the Partnership. The partnership agreement also grants the limited partners holding Class A Units certain rights and remedies in the "event of default" by the Partnership, the Subsidiary or Industries, including the right to purchase the assets of the Partnership or the Subsidiary's interest in the Partnership for fair market value, based upon an independent MAI appraisal, or to dissolve the Partnership. Under the limited partnership agreement of the Partnership an event of default includes a withdrawal of the Subsidiary as general partner, a bankruptcy, assignment for the benefit of creditors, receivership or dissolution of the Subsidiary or Industries, or breach of certain financial covenants by the Subsidiary or Industries. Upon an event of default, the Subsidiary's interest in the Partnership will be converted automatically to that of a limited partner. Any limited partnership interest held by the Subsidiary, upon conversion of the Subsidiary to a limited partner in the event of default or otherwise, will be represented by Class B Units. The voting rights of the Class B

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

Units are generally one-tenth of those of the Class A Units. The Subsidiary has also pledged its interest in the Partnership as collateral for payment of the loans from the limited partners to the Partnership, as well as performance of the Partnership's and the Subsidiary's obligations under the partnership agreement.

As Industries, through the Subsidiary, owns a majority interest in the office building, Industries' consolidated financial statements include the assets, liabilities and the operating results of the building since the date of acquisition.

The unaudited pro forma consolidated results of operations which follow, assume that the acquisition had occurred as of January 1 in each of the periods presented.

	(in thousands, except per share amounts)	
	1987	1986
Revenues	\$ 886	1,060
Net earnings (loss)	\$(847)	(718)
Earnings (loss) per share	\$ (.85)	(.71)

The pro forma financial information is not necessarily indicative either of results of operations that would have occurred had the purchase been made at the beginning of the period or of future results of operations of Industries, the Partnership or the presentation of the combined results hereof.

(12) Information on Segments of Business

Industries' significant business segments are presented below:

Real Estate

Industries' wholly owned subsidiary, 550 POB, Inc., is general partner and has a 55.6% interest in a limited partnership which during November 1987 purchased an office building. The building has total office space of approximately 53,700 net rentable square feet and is approximately 75% leased currently.

Manufacturing

Industries' manufacturing subsidiary, Metals, fabricates custom specialty dials. These dials are used as components for watches, clocks and timers for consumer and automotive applications.

Equity Ownership

Industries has an ownership interest in Pinnacle which is accounted for under the equity method of accounting. At December 31, 1987, Industries' ownership position in Pinnacle Common Stock represented approximately 44% of the total number of shares of Pinnacle Common Stock outstanding.

	(in thousands) Year Ended December 31, 1987
Sales and other income:	
Real estate	\$ 44
Manufacturing	367
Other	162
	<u>\$ 573</u>
Earnings (loss) from continuing operations:	
Real estate	\$ (39)
Manufacturing	74
Equity ownership	(544)
Other	(265)
	<u>\$ (744)</u>
Identifiable assets:	
Real estate	\$2,926
Manufacturing	347
Equity ownership	1,638
Other	923
	<u>\$5,834</u>
Depreciation and amortization:	
Real estate	\$ 10
Manufacturing	7
Other	65
	<u>\$ 82</u>
Capital expenditures:	
Real estate	\$2,938
Manufacturing	4
	<u>\$2,942</u>

REPORT OF INDEPENDENT CERTIFIED PUBLIC ACCOUNTANTS

To the Board of Directors and
Stockholders of USR Industries, Inc:

We have examined the consolidated balance sheets of USR Industries, Inc. and subsidiaries as of December 31, 1987 and 1986, and the related consolidated statements of operations, stockholders' equity and changes in financial position for each of the three years in the period ended December 31, 1987. Our examinations were made in accordance with generally accepted auditing standards and, accordingly, included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

As discussed in Note 10 to the consolidated financial statements, there exists certain litigation, the outcome of which cannot presently be determined.

In our opinion, subject to the effects on the financial statements of such adjustments, if any, as might be required had the outcome of the uncertainties referred to in the preceding paragraph been known, the consolidated financial statements referred to above present fairly the financial position of USR Industries, Inc. and subsidiaries as of December 31, 1987 and 1986 and the results of their operations and the changes in their financial position for each of the three years in the period ended December 31, 1987, in conformity with generally accepted accounting principles applied on a consistent basis.

Coopers & Lybrand

Houston, Texas
March 29, 1988

SELECTED FINANCIAL DATA

The following selected condensed financial information has been derived from, and is qualified by reference to and should be read in conjunction with, Industries' Consolidated Financial Statements and Notes thereto included elsewhere herein, except the data relating to the fiscal years ended December 31, 1984 and 1983 which has been derived from previously published financial statements.

	(in thousands except per share amounts) Years Ended December 31,				
	1987	1986	1985	1984	1983
Revenues	\$ 573	490	359	342	664
Net earnings (loss) from continuing operations	\$ (773)	(695)	(538)	(641)	281
Net earnings (loss) per share from continuing operations	\$ (.78)	(.69)	(.52)	(.61)	.24
Total assets	\$5,834	4,067	4,911	6,050	7,319
Total current liabilities	\$ 755	581	748	1,346	1,735
Long-term obligations	\$2,097	64	—	—	65
Stockholders' equity	\$2,613	3,388	4,163	4,704	5,584

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

LIQUIDITY AND CAPITAL RESOURCES

To date Industries had funded its internal cash needs from operations; collection of accounts receivable and other current accounts as well as through asset sales; issuance of common stock; and bank borrowings from time to time. Effective December 31, 1986, Industries terminated its two defined benefit pension plans and, in connection with such terminations, recorded a receivable of approximately \$690,000 to reflect the recovery of assets in excess of the accumulated plan benefits and costs associated with plan terminations. The distribution of excess assets and collection of the receivable took place during the third quarter of 1987. With the sales of Industries' manufacturing assets and its Plan of Asset Redeployment having been substantially completed, Industries expects to look to sales of assets to meet its liquidity needs, if such are not met from current operations.

On a consolidated reporting basis as of December 31, 1987, Industries' working capital deficit was \$40,663 and the ratio of current assets to current liabilities was .9:1 versus working capital of \$261,576 and current ratio of 1.5:1 as of December 31, 1986. Management anticipates that during 1988 Industries may require additional sources of liquidity. To meet its liquidity requirements or in connection with other corporate objectives Industries may sell assets, offer additional securities or incur additional indebtedness.

In addition to usual transactional and operating costs, Industries has been required to bear very substantial administrative and legal expenses for certain environmental litigation. For further discussion as to environmental regulations and litigation see Notes to Consolidated Financial Statements and Note 10 thereof. Under a Defense Agreement dated September 30, 1985 to which Industries, SLC and five primary insurance carriers are parties, certain of

Industries' ongoing legal defense costs in the environmental litigation have been assumed by such insurance carriers. However, the Defense Agreement does not fully cover either the direct or indirect costs of Industries of the litigation. Further, it should be noted that the insurance carriers are defending "under reservation" of their absolute right to deny all liability on the underlying claims.

Industries is subject to additional environmental claims which are not covered by any defense agreement with insurers, although negotiations for the possible participation by certain insurance carriers are in progress. Of course there can be no assurance that such discussions will result in any agreement as to defense costs. In the event that no agreement is reached with insurers with respect to such defense costs, Industries will be required to provide for additional legal expenses. Potential sources of liquidity for Industries include sales of the Common Stock of Pinnacle and discounting of notes receivable from the Purchasing Corporations.

Industries anticipates that during 1988 it may bolster its liquidity by offering its stockholders the right to purchase certain shares of Pinnacle Common Stock.

RESULTS OF OPERATIONS

1987 Compared With 1986

Total revenues during 1987 increased to \$573,295 from \$490,331 in 1986. Manufacturing sales for the year ended December 31, 1987 were \$367,446 compared to \$337,631 for the comparable prior year. The increase of \$29,815 is primarily attributable to increased prices and unit sales volume. Interest income of \$61,517 for the current year, derived primarily from notes receivable from the sale of certain net assets of Lighting and Metals, increased \$6,805 from the prior year.

Cost of sales for the current year was \$140,171 compared to \$186,637 for the year ended December 31, 1986. Decreased costs of sales primarily reflect a reduction in direct labor costs. Selling, general and administrative expenses for the year ended December 31, 1987 were \$579,822 compared to \$462,417 for the prior year. The increase reflects nonrecurring expenses in connection with the purchase and operations of the office building at 550 Post Oak Boulevard, Houston, Texas 77027 offset by continued reductions in corporate overhead expenses. Industries' expenses for 1986 are net of reimbursement of certain prior costs made by five primary insurance carriers pursuant to a Defense Agreement dated September 30, 1985. Interest expense for the current year increased \$46,823 from \$23,891 reflecting interest expense for approximately two months on the mortgage assumption connected with the office building purchase.

Effective December 31, 1986 Industries terminated its two defined benefit pension plans for receivable of \$690,000 was recorded to reflect the recovery of assets in excess of the accumulated plan benefits and costs associated with plan terminations. Such receivable was collected in full during the third quarter of 1987.

Industries' equity in the net loss of Pinnacle of \$352,686 reflects Industries' pro rata share of Pinnacle's results of operations for 1987. The decrease from 1986 is due primarily to Pinnacle not incurring any further writedowns of its producing oil and gas properties during 1987. In addition, Industries recorded a \$192,000 writedown on shares of Pinnacle Common Stock anticipated to be

offered by Industries to its stockholders through a rights offering to be made during 1988.

Primarily as a result of the foregoing factors Industries reported a net loss of \$773,568 for 1987.

1986 Compared With 1985

Total revenues during 1986 increased to \$490,331 from \$358,826 in 1985. Manufacturing sales for the year ended December 31, 1986 were \$337,631 compared to \$246,411 for the comparable prior year. The increase of \$91,220 is primarily attributable to increased unit sales volume. Interest income of \$54,712 for 1986, derived primarily from notes receivable from the sales of certain net assets of Lighting and Metals, decreased \$7,132 from the prior year.

Cost of sales for 1986 was \$186,637 compared to \$139,132 for the year ended December 31, 1986. Increased cost of sales resulted from increased sales volume during 1986 compared to the prior year. Selling, general and administrative expenses for the year ended December 31, 1986 were \$462,417 compared to \$342,710 for the prior year. Industries' expenses for 1985 are net of reimbursement of certain prior costs made by five primary insurance carriers pursuant to a Defense Agreement dated September 30, 1985. Interest expense for 1986 decreased \$16,134 to \$23,891, reflecting lower interest rates during the year.

Industries made no sales of Pinnacle Common Stock during 1986 and realized no gain or loss therefrom during 1986. During 1985 a loss of \$67,905 was realized in connection with the sale of Pinnacle Common Stock. Effective December 31, 1986 Industries terminated its two defined benefit pension plans and a receivable of \$690,000 was recorded to reflect the estimated net reversion to Industries of surplus assets of such pension plans.

Industries equity in the net loss of Pinnacle of \$1,110,654 reflects Industries' pro rata share of Pinnacle's results of operations for 1986. During 1986, Pinnacle's results were adversely affected by the continuation of lower oil and gas prices and writedowns of its oil and gas properties. There were no losses from discontinued operations for 1986 compared to a loss of \$19,057 in 1985. The loss for discontinued operations in 1985 reflect approximately six weeks of manufacturing operations through February 13, 1985.

The 1986 loss of \$695,468 is higher than the loss of \$557,411 sustained in 1985, primarily as a result of an increased equity pickup of \$903,001 in the net loss of Pinnacle offset by a gain of \$690,000 recognized on termination of two defined benefit pension plans.

INFLATION AND CHANGES IN PRICES

In recent years Industries' ownership interest have operated in sectors having generally deflationary economic environments. The impact of inflation on the revenues and expense levels reported by Industries during the past three years have been insignificant. In the event that domestic inflationary pressures reoccur management believes that Industries' ownership interests in the real estate and natural resources sectors, which traditionally have been viewed as hedges against inflation, will be relatively well positioned to adjust for inflation and changes in prices. Management expects the oil and gas prices may trend upwards during 1988 but of course no assurance can be offered as to such trends. With easing of inflationary pressures during recent years, both the selling prices for Industries' manufactured products and the costs of production, including costs of labor and materials, have tended to stabilize. However, despite declines in the U.S. dollar relative to most Asian currencies during 1987, competition in the Metals' business from Asian based exporters remains intense.

PRINCIPAL MARKET AND STOCK PRICES

The following table sets forth the range of sales prices on the American Stock Exchange ("Amex") for Industries' Common Stock for each quarter during the last two fiscal years. With the cooperation of the Amex, during January 1988 Industries voluntarily delisted from the Amex and trading for its common stock was established on the National Automated Quotation System under the symbol "UIND".

	<u>High</u>	<u>Low</u>
1987		
First Quarter	\$2.251	\$1.625
Second Quarter	1.875	1.375
Third Quarter	2.25	1.25
Fourth Quarter	2.125	1.00
1986		
First Quarter	\$3.125	\$2.125
Second Quarter	3.375	2.625
Third Quarter	3.00	1.625
Fourth Quarter	2.00	1.625

APPROXIMATE NUMBER OF HOLDERS OF COMMON STOCK

At March 1, 1988 there were approximately 1,400 holders of record of Common Stock of Industries.

DIVIDEND INFORMATION

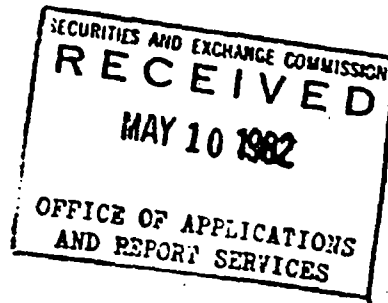
No cash dividends were declared or paid during the two year period ended December 31, 1987. Management believes it unlikely that Industries will pay dividends in the foreseeable future.

ANNUAL REPORT ON FORM 10-K

The Annual Report on Form 10-K for the year ended December 31, 1987 is available to stockholders without charge upon written request to the Company at 550 Post Oak Boulevard, Suite 525, Houston, Texas 77027.

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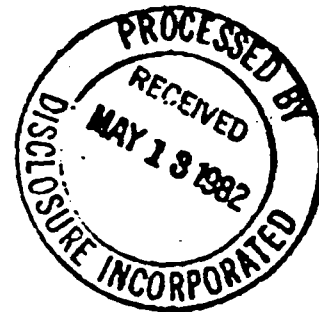
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USR INDUSTRIES, INC.

ORIGINAL
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Annual Report

1981

XXIX-010

USR INDUSTRIES, INC.

Directors

BRIAN P. BURNS

Principal Occupation or Employment
Partner in the law firm of Burns & Whitehead;
Chairman of Boothe Financial Corporation

JOSEPH G. KOSTRZEWA

President of Traverse
Oil Company

RALPH T. McELVENNY, Jr.

Chairman and President of the Company;
Chairman of Titan Wells, Inc.

Officers

RALPH T. McELVENNY, Jr.

Chairman of the Board and President

WILLIAM C. KALTNECKER

Treasurer and Secretary

WILLIAM E. CRIQUI

Assistant Treasurer

Transfer Agent

MANUFACTURERS HANOVER TRUST CO.,
NEW YORK, N.Y.

Registrar

CHEMICAL BANK, NEW YORK, N.Y.

Counsel

O'MELVENY & MYERS, LOS ANGELES, CALIFORNIA

HANNOCH, WEISMAN, STERN, BESSER
BERKOWITZ & KINNEY, NEWARK, NEW JERSEY

Auditors

PEAT, MARWICK, MITCHELL & CO.,
SHORT HILLS, N.J.

Corporate Headquarters

2203 TIMBERLOCH PLACE
THE WOODLANDS, TEXAS 77380

Equal Employment Opportunity Policy

USR Industries, Inc. is an equal opportunity employer, and its policy is not to discriminate against any employee or applicant for employment because of race, color, religion, sex or national origin.

TO OUR STOCKHOLDERS:

Regretably, for the year ended December 31, 1981, USR Industries, Inc. (the "Corporation") sustained a net loss totaling \$321,716 (\$.28 per share) after a net loss of \$474,317 (\$.41 per share) during the fourth quarter. For the prior year ended December 31, 1980, the Corporation sustained a net loss of \$335,530 (\$.29 per share) after a net loss of \$170,271 (\$.15 per share) during the fourth quarter. Results for 1981 include adjustment for operations discontinued during 1981 or held for disposition as of the year end. During 1981 the Corporation recognized a loss of \$86,181 (\$.08 per share) from continuing operations on revenues of \$3,616,406 compared to a loss during the prior year of \$358,311 (\$.31 per share) from continuing operations on revenues of \$3,189,290.

Comments on Results

Despite intense efforts by management operating results for 1981 were disappointing. However, we believe that through these efforts we have made substantial progress in laying the foundation to complete asset redeployment into sectors believed to offer stronger growth potential and future prospects for the Corporation and its shareholders.

The most significant event of the past year was divestiture of the business of the Corporation's former subsidiary, USR Chemicals, Inc., by sale of the subsidiary's assets to Mitsubishi Chemical Industries Limited during the summer. Also of note during 1981, the Corporation purchased just under five percent of the common stock of Boothe Financial Corporation, a San Francisco based company with substantial cash reserves that is active in real estate and the financial services industry, and agreed to purchase an equity participation in Titan Wells, Inc., a company active in the important field of natural resource exploration and production.

Asset Redeployment Program

The primary objective of the Corporation's asset redeployment program is to review and restructure operations to improve future performance. Talented and devoted management personnel are important to the success of any business. However, at some junctures during the development of a business the most important contribution by management may be to choose business sectors which are themselves healthy and present opportunities for growth.

In recent years, many have recognized that the markets for the products of certain basic American industries, such as the steel and automotive industries, are not healthy. Similarly, the Corporation's stockholders should be aware that the principal markets for products of the Corporation's subsidiaries—the television, automotive and watch industries—also are not healthy. Indeed, these industries have not enjoyed general prosperity for several years. The asset redeployment plan is intended to prune back the Corporation's exposure to business sectors deemed less desirable and to substantially increase participation in new sectors believed to offer a stronger future and improved growth potential.

The broad outlines of the Corporation's asset redeployment program were established during late 1978. However, broad plans set forth objectives which can be achieved only through specific steps. Management is actively considering specific proposals to fulfill the business purposes of the Corporation's asset redeployment plan. Additional actions or proposals are expected to be communicated or presented for shareholder consideration as soon as practicable.

Divestiture of the Chemical Products Business: An Example of the Need for Redeployment

Sale of the chemical products business referred to above was motivated by several considerations. Many small manufacturing businesses face difficult problems in the current economic climate. Although the chemical products subsidiary did enjoy periods of success in recent years, its overall record was unsatisfactory and future prospects appeared limited. The large consumer electronics companies which constitute the subsidiary's principal customers were subject to intense price competition, fragmentation of market share and political pressure to maintain full employment despite softening economic conditions. Other factors also adversely affected the subsidiary's business, including the relatively high cost of manufacturing in the United States as compared to many areas of the world, disadvantageous international trade agreements entered into by the United States and general public antagonism against American corporations. Fifteen years ago, worldwide manufacturing and assembly of color television tubes and components were centered in the United States. Today, largely in response to the foregoing problems, the centers of this substantial industry have moved to Asia and Western Europe.

The foregoing difficulties may be responded to more effectively by large multi-national companies than by a small domestic manufacturer such as the Corporation. Accordingly, management was pleased to sell the subsidiary's assets to a well managed, strongly financed, international company, Mitsubishi Chemical Industries Limited. We wish our former employees, customers and the many friends of our chemical products subsidiary every future success.

1981 Annual Meeting

Although a full Annual Report and audited financial statements were regularly mailed to stockholders, no 1981 Annual Meeting was held. The Corporation was involved intensely in the sale of the business of its chemical products subsidiary during the months immediately preceeding and following the scheduled 1981 Annual Meeting. The agreement for sale of the business of the chemical products subsidiary was executed as of May 31, 1981. Primary payment was made thereunder on June 15, 1981 while a later adjusting payment, arrangements to provide for transfer of employee benefit programs, final internal accounting and other matters arising in connection with the transaction continued for a number of months thereafter.

In addition to the need for uninterrupted concentration on the important negotiations concerning the sale of the chemical products business described above, the Directors were also considering a proposal to establish an international domicile for the Corporation. Management believed, however, that such proposal should not be submitted for stockholder review unless appropriate advance rulings had been obtained to clarify the government's position as to interpretation of applicable tax regulations. Unfortunately, requests for governmental rulings required considerably greater time and effort than had been anticipated.

Originally it was intended to reschedule the 1981 Annual Meeting after advice was received from the government with respect to applicable tax regulations and materials could be finalized for submission to shareholders concerning an international domicile for the Corporation. Because the decision not to pursue such course at that time was not made until late in 1981 and the asset sale of the chemical products subsidiary required intense effort during several months in a row, management concluded that it was advisable to look toward the regular 1982 Annual Meeting to consider matters that would have been addressed in the prior year.

New Office Location

In consonance with the intended emphasis on the natural resources sector, the Corporation has relocated its corporate office facilities to the heart of the natural resources industry. The Corporation has selected a modest but well located facility in The Woodlands, Texas, a commercial office and home development project established only a few years ago under sponsorship of a major independent energy and real estate development company. Many corporations, including prominent energy companies, already are operating in this area. Management believes that this location and business environment can assist the Company in realizing its potential.

In Appreciation

On behalf of both management and the Board of Directors, I wish to thank our employees, professional advisors and other friends for their many contributions. We hope that the long term performance of the Corporation will justify the confidence and hopes embodied in the plan for asset redeployment.

Sincerely,

A handwritten signature in dark ink, appearing to read "Ralph T. McElvenny, Jr.", written in a cursive style.

Ralph T. McElvenny, Jr.
Chairman of the Board

USR INDUSTRIES, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF OPERATIONS

Years ended December 31, 1981, 1980 and 1979

	1981	1980	1979
Revenues:			
Net sales	\$3,380,932	3,040,498	2,765,174
Other income	235,474	148,792	95,725
Total revenues	<u>3,616,406</u>	<u>3,189,290</u>	<u>2,860,899</u>
Costs and expenses:			
Cost of sales	2,556,435	2,394,598	2,184,708
Selling, administration and general expenses	1,126,890	1,242,896	1,180,396
Interest expense	19,262	7,107	31,029
Total costs and expenses	<u>3,702,587</u>	<u>3,644,601</u>	<u>3,396,133</u>
Loss from continuing operations before income taxes and extraordinary item	(86,181)	(455,311)	(535,234)
Income tax (benefit)	—	(97,000)	—
Loss from continuing operations before extraordinary item	<u>(86,181)</u>	<u>(358,311)</u>	<u>(535,234)</u>
Discontinued operations:			
Earnings from operations of discontinued businesses (less applicable income taxes of \$38,800 in 1981, \$10,500 in 1980 and \$630,000 in 1979)	44,397	12,281	734,030
Loss on disposal of discontinued businesses (including income taxes of \$86,300)	(385,032)	—	—
Earnings (loss) from discontinued operations	<u>(340,635)</u>	<u>12,281</u>	<u>734,030</u>
Earnings (loss) before extraordinary item	<u>(426,816)</u>	<u>(346,030)</u>	<u>198,796</u>
Extraordinary item—tax benefit from net operating loss carryforward	105,100	10,500	492,000
Net earnings (loss)	<u>\$ (321,716)</u>	<u>(335,530)</u>	<u>690,796</u>
Earnings (loss) per share:			
Loss from continuing operations before extraordinary item	\$ (.08)	(.31)	(.48)
Earnings (loss) from discontinued operations	(.29)	.01	.63
Earnings (loss) before extraordinary item	(.37)	(.30)	.17
Extraordinary item	.09	.01	.42
Net earnings (loss)	<u>\$ (.28)</u>	<u>(.29)</u>	<u>.59</u>
Weighted average number of common shares and common share equivalents	<u>1,163,919</u>	<u>1,164,136</u>	<u>1,168,013</u>

See accompanying notes to consolidated financial statements.

USR INDUSTRIES, INC. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

December 31, 1981 and 1980

ASSETS

	1981	1980
Current assets:		
Cash, including short-term investments of \$1.4 million in 1981	\$1,633,505	466,546
Receivables:		
Trade accounts, less allowance for doubtful accounts of \$20,780 in 1981 and \$24,532 in 1980	565,536	605,629
Other receivables	78,854	25,115
Net receivables	644,390	630,744
Inventories	329,618	393,904
Prepaid expenses	41,110	69,174
Net current assets of discontinued businesses	64,395	2,522,394
Total current assets	2,713,018	4,082,762
Ownership of non-consolidated subsidiary	511,308	960,564
Other investments	2,319,154	351,260
Property, plant and equipment, at cost	2,076,153	2,050,206
Less accumulated depreciation and amortization	1,641,416	1,548,240
Net property, plant and equipment	434,737	501,966
Net non-current assets of discontinued businesses	216,550	904,214
Other assets	1,911	4,315
	\$6,196,676	6,805,081

LIABILITIES AND STOCKHOLDERS' EQUITY

Current liabilities:		
Current installments under capital lease	\$ 449	418
Accounts payable—trade	199,836	445,477
Accrued expenses:		
Salaries and wages	133,500	55,799
Pensions	82,047	88,928
Professional fees	115,500	159,925
Other	227,749	195,738
Total accrued expenses	558,796	500,390
Income taxes	7,385	7,385
Total current liabilities	766,466	953,670
Long-term obligations under capital lease excluding current installments	68,271	68,720
Stockholders' equity:		
Common stock of \$1 par value per share.		
Authorized 3,500,000 shares; issued 1,168,698, less 7,162 shares in 1981 and 4,562 shares in 1980 held in treasury	1,161,536	1,164,136
Additional paid-in capital	856,257	858,843
Retained earnings	3,506,146	3,827,862
Less: allowance for net unrealized loss on non-current marketable equity securities	(160,000)	(68,150)
Total stockholders' equity	5,363,939	5,784,691
	\$6,196,676	6,805,081

See accompanying notes to consolidated financial statements.

USR INDUSTRIES, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY
Years ended December 31, 1981, 1980 and 1979

	<u>1981</u>	<u>1980</u>	<u>1979</u>
Common stock(1)			
Balance at beginning of year (1,164,136 shares in 1981; 1,114,136 in 1980; 1,114,138 in 1979)	\$1,164,136	1,114,136	1,114,138
Treasury stock acquired	(2,600)	—	(2)
Issuance of stock in purchase transaction	—	50,000	—
Balance at end of year (1,161,536 shares in 1981; 1,164,136 in 1980; 1,114,136 in 1979)	<u>\$1,161,536</u>	<u>1,164,136</u>	<u>1,114,136</u>
Additional paid-in capital			
Balance at beginning of year	\$ 858,843	783,843	783,841
Treasury stock acquired	(2,586)	—	2
Issuance of stock in purchase transaction	—	75,000	—
Balance at end of year	<u>\$ 856,257</u>	<u>858,843</u>	<u>783,843</u>
Retained earnings			
Balance at beginning of year	\$3,827,862	4,163,392	3,472,596
Net income (loss)	(321,716)	(335,530)	690,796
Balance at end of year	<u>\$3,506,146</u>	<u>3,827,862</u>	<u>4,163,392</u>
Allowance for loss on non-current marketable equity securities			
Balance at beginning of year	\$ (66,150)	—	—
Net unrealized loss	(93,850)	(66,150)	—
Balance at end of year	<u>\$ (160,000)</u>	<u>(66,150)</u>	<u>—</u>
Total stockholders' equity			
Balance at beginning of year	\$5,784,691	6,061,371	5,370,575
Net change during the year	(420,752)	(276,680)	690,796
Balance at end of year	<u>\$5,363,939</u>	<u>5,784,691</u>	<u>6,061,371</u>

(1) Net of common stock in treasury of 7,162 shares at December 31, 1981 and 4,562 shares at December 31, 1980 and 1979.

See accompanying notes to consolidated financial statements.

USR INDUSTRIES, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CHANGES IN FINANCIAL POSITION

Years ended December 31, 1981, 1980 and 1979

	1981	1980	1979
SOURCES OF WORKING CAPITAL:			
Continuing operations:			
Loss from continuing operations	\$ (86,181)	(358,311)	(535,234)
Items which do not use (provide) working capital:			
Depreciation and amortization	99,452	87,311	93,914
Deferred income taxes (benefit)	—	(97,000)	97,000
Equity in earnings of non-consolidated subsidiary	(69,492)	(138,260)	(59,288)
Working capital provided by (used for) continuing operations	(56,221)	(506,260)	(403,608)
Discontinued operations:			
Earnings (loss) from discontinued operations	(340,635)	12,281	734,030
Items which do not use (provide) working capital:			
Depreciation and amortization	103,310	184,835	188,082
Net book value of non-current assets of discontinued operations	584,354	(81,884)	(182,628)
Working capital provided by discontinued operations	347,029	115,232	739,484
Working capital provided by (used for) continuing and discontinued operations	290,808	(391,028)	335,876
Issuance of common stock to acquire investment	—	125,000	—
Extraordinary item	105,100	10,500	492,000
Return of capital and interest payment from non-consolidated subsidiary	518,750	237,500	—
Loss on disposition and write-downs of machinery, equipment and other assets	—	9,909	13,678
Proceeds from sale of machinery and equipment	—	3,360	2,000
Other	2,121	(1,607)	(1,327)
Decrease in working capital	1,182,540	417,021	414,067
	<u>\$ 2,099,319</u>	<u>410,655</u>	<u>1,256,294</u>
USES OF WORKING CAPITAL:			
Additions to plant and equipment	\$ 31,940	186,137	37,352
Decrease in long-term lease obligations	449	418	25,632
Investment in non-consolidated subsidiary	—	—	1,000,000
Expenditures for other investments	2,061,744	224,100	193,310
Treasury stock acquired	5,186	—	—
	<u>\$ 2,099,319</u>	<u>410,655</u>	<u>1,256,294</u>
CHANGES IN COMPONENTS OF WORKING CAPITAL:			
Increase (decrease) in current assets:			
Cash	\$1,166,959	(374,801)	326,987
Receivables	13,645	66,499	(178,517)
Inventories	(64,286)	(28,897)	111,754
Prepaid expenses	(28,064)	24,370	12,094
Net current assets of discontinued operation	(2,457,999)	(257,878)	(176,990)
	(1,369,744)	(570,707)	95,328
Increase (decrease) in current liabilities:			
Current installments under capital lease	31	(25,214)	996
Accounts payable—trade	(245,641)	134,402	120,911
Other current liabilities	—	(140,263)	140,263
Accrued expenses	58,406	(18,168)	206,226
Income taxes	—	(104,443)	40,999
	(187,204)	(153,686)	509,395
Decrease in working capital	<u>\$ (1,182,540)</u>	<u>(417,021)</u>	<u>(414,067)</u>

See accompanying notes to consolidated financial statements.

USR INDUSTRIES, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 1981, 1980 and 1979

(1) Summary of Significant Accounting Principles

(a) Financial Statement Reclassification

The accompanying consolidated financial statements for USR Industries, Inc. ("Industries") and subsidiaries have been reclassified to reflect the planned disposition of Industries' wholly owned subsidiary, Safety Light Corporation ("SLC"), the sale during 1981 of the net assets and business of Industries' wholly owned subsidiary USR Chemicals, Inc. ("Chemicals") and to classify their respective operations as discontinued. See also note 2 ("Discontinued Operations"). Except as otherwise indicated, all financial information relates to continuing operations.

(b) Principles of Consolidation

The consolidated financial statements include the accounts of USR Industries and its wholly owned subsidiaries USR Lighting, Inc. ("Lighting") and USR Metals, Inc. ("Metals"). Accounts relating to the operations of Chemicals and SLC are included in the consolidated financial statements as discontinued businesses. Investment in a non-consolidated, wholly owned subsidiary, Unatco Funding Corporation ("Unatco"), is stated at cost plus equity in that subsidiary's earnings since its inception in 1979.

All material intercompany accounts and transactions have been eliminated in consolidation.

(c) Inventories

Inventories of raw materials are priced at the lower of cost (first-in, first-out) or replacement market. Work-in-process and finished goods inventories are valued at the lower of average cost or market (replacement cost or net realizable value).

(d) Property, Plant and Equipment

Depreciation and amortization are provided on a straight-line basis, in amounts sufficient to write-off the cost of depreciable assets over their estimated useful lives.

Expenditures for maintenance and repairs are charged to costs and expenses as incurred. Expenditures for renewals and betterments are capitalized. It is the policy of Industries and its subsidiaries to relieve the asset accounts and related accumulated depreciation of assets abandoned, sold, retired or

otherwise disposed of and to include in current operations any gains or losses realized thereon.

(e) Income Taxes

Deferred income taxes are recorded to reflect the effect of timing differences in computing income for financial reporting and income tax purposes. Industries and its subsidiaries account for investment tax credits using the flow-through method.

(f) Earnings (Loss) Per Share

Net earnings (loss) per common share are based on the weighted average number of outstanding shares and equivalent shares from dilutive stock options. In 1979, the earnings per common share assuming full dilution is the same as earnings per common share. The assumed exercise of stock options in 1981 and 1980 would be anti-dilutive.

(g) Research and Development

Research and development expenditures are charged to operations as incurred. Total research and development expenses during the years ended December 31, 1981, 1980 and 1979 were \$63,750, \$68,063 and \$60,200 respectively.

(2) Discontinued Operation

On June 15, 1981, Industries sold certain assets owned by or used in the business of Chemicals to Mitsubishi Chemical Industries Ltd., a Japanese corporation, for a purchase price of approximately \$2.4 million.

Pursuant to a plan approved by the Board of Directors on December 15, 1981, Industries intends to sell the stock of its wholly owned subsidiary SLC and certain assets of USR Metals, Inc. to a group lead by current executive officers of SLC at a purchase price of approximately \$350,000 (including an 8% secured promissory note of \$315,000 payable over 8 years). The transaction is expected to be completed during 1982.

Net loss on disposal of discontinued business represents the estimated loss of \$460,000 resulting from the ultimate disposition of SLC less net gain of \$161,300 before income taxes of \$66,300 from the sale of Chemicals.

The consolidated balance sheet at December 31, 1980 includes net assets of discontinued operations at cost; while the Consolidated Balance Sheet at December 31, 1981 includes such items at their estimated net realizable value.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The operations of Chemicals and SLC are reported in the accompanying consolidated statements of operations as discontinued operations. Such amounts include net sales of \$2,073,582 in 1981; \$5,222,943 in 1980 and \$8,798,923 in 1979.

(3) Corporate Restructuring

The financial statements for 1979 relate to United States Radium Corporation ("USRC"). Pursuant to an Agreement and Plan of Merger dated May 16, 1980 and approved by shareholders of USRC, on August 27, 1980 a newly formed subsidiary of Industries was merged into USRC on a basis whereby shares of common stock of USRC were deemed to have been converted share for share into shares of common stock of Industries.

(4) Inventories

Stated values of inventories include costs of material, labor and manufacturing overhead related to purchases or production cost. The components of inventories are as follows:

	December 31	
	1981	1980
Raw material	\$113,831	117,643
Work-in-process	215,787	276,261
	<u>\$329,618</u>	<u>393,904</u>

Finished goods are not significant because such items are shipped and billed to customers upon completion.

(5) Ownership of Non-Consolidated Subsidiary

Industries' investment in Unatco is shown as a non-consolidated subsidiary reflecting Unatco's intent primarily to invest in and finance ventures and to distinguish its business as being substantially different from that of Industries, which is primarily involved in manufacturing. Condensed financial data of Unatco is presented below.

UNATCO FUNDING CORPORATION CONDENSED BALANCE SHEETS

December 31, 1981 and 1980

	1981	1980
ASSETS		
Cash	\$ —	21,238
Short-term investments	511,459	936,984
Interest receivable	560	2,342
	<u>\$512,019</u>	<u>960,564</u>

LIABILITIES AND STOCKHOLDERS' EQUITY

Current liabilities:

Interest and accounts payable due parent company	\$ 15,000	14,054
Accrued expenses	2,345	1,831
	<u>17,345</u>	<u>15,885</u>

Convertible subordinated debentures	200,000	500,000
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Stockholders' equity:

Capital stock	100,000	300,000
Retained earnings	194,674	144,679
Total stockholders' equity	<u>294,674</u>	<u>444,679</u>
	<u>\$512,019</u>	<u>960,564</u>

All outstanding convertible subordinated debentures were owned by Industries at December 31, 1981.

CONDENSED STATEMENTS OF EARNINGS

Years ended December 31, 1981 and 1980 and
six months ended December 31, 1979

	1981	1980	1979
Interest income	\$71,845	138,361	61,033
Cost and expenses (including parent company interest charges)	21,849	32,331	22,324
Net earnings ⁽¹⁾	<u>\$49,996</u>	<u>105,970</u>	<u>38,709</u>

⁽¹⁾ For U.S. income tax purposes, all of the net earnings of Unatco are included as gross income to Industries. For financial reporting purposes, Unatco's net earnings are included in other income in the consolidated statements of operations of Industries.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(6) Property, Plant and Equipment

A summary of property, plant and equipment at December 31, 1981 and 1980 is as follows:

	1981	1980
Building and building equipment	\$ 183,254	183,254
Machinery and equipment	1,561,127	1,510,389
Office furniture and fixtures	123,335	120,494
Leasehold improvements	192,419	151,482
Construction-in-progress	16,018	84,587
	<u>\$2,076,153</u>	<u>2,050,206</u>

(7) Pension Plan

Industries and its subsidiaries have in effect several pension plans which together cover substantially all employees. Total pension expense was \$53,687, \$46,360, and \$61,869 for the years 1981, 1980 and 1979 respectively. Included in pension expense is the amortization of past service costs over a maximum of 40 years. Industries makes annual contributions to the plans equal to the amounts accrued for pension expense. Accumulated plan benefits and net assets available for benefits as of January 1, 1981 and 1980 (the most recent actuarial valuation dates) is presented below:

	January 1	
	1981	1980
Actuarial present value of accumulated plan benefits:		
Vested	\$2,168,321	1,956,274
Non Vested	125,713	115,089
	<u>\$2,294,034</u>	<u>2,071,363</u>
Net assets available for benefits	<u>\$2,017,076</u>	<u>1,782,359</u>

The weighted average assumed rate of return used in determining the actuarial present value of accumulated plan benefits was 8 per cent for 1981 and 1980.

Changes in the actuarial assumptions used in computing pension expense, for continuing and discontinued operations during 1980 and 1979 had the effect of reducing such expense by approximately \$36,000 in 1980 and \$41,000 in 1979 below the level which would have resulted under the assumptions applied in prior years.

(8) Income Taxes

The tax provision differs from the amounts of "expected" tax provision computed by applying the

applicable statutory income tax rate to the earnings (loss) from continuing operations before income taxes and extraordinary item, as shown below:

	1981	1980	1979
Computed "expected" tax benefit	\$(40,000)	(209,000)	(246,000)
Dividend received exclusion	(16,300)	—	—
Book loss carryforward for which no current tax benefit is available	56,300	209,000	246,000
Application of book loss carryforward to deferred tax credit	—	(97,000)	—
Income tax credit	<u>\$ —</u>	<u>(97,000)</u>	<u>—</u>

In 1981 Industries recognized a tax expense of \$125,100 related to the earnings from discontinued operations of \$83,200 and a gain on the disposal of Chemicals of \$161,000. The difference between the tax provided and the tax computed at the statutory rate of 46% is comprised of recaptured tax and state income taxes net of Federal tax benefit. An extraordinary item of \$105,100 has been recognized for the tax benefit of net operating loss carryforward utilized for financial statement purposes. The tax benefit of the estimated loss on the disposal of SLC will be recognized in the future as an extraordinary item at the time such loss reduces income tax liability. For 1980 and 1979 income taxes related to discontinued operations have been reclassified; such reclassifications have no effect on net earnings (loss) for such years.

Taxes currently payable consist of Federal income taxes payable of \$4,000 representing recaptured tax and state income taxes of \$16,000 applicable to discontinued operations in 1981. There were no taxes payable in 1980. In 1979 current taxes payable were \$22,000 relating to state income taxes for discontinued operations.

In 1980, for financial statement purposes the tax effect of the operating loss has been recognized by eliminating the deferred tax credit of \$97,000 which arose in a prior year. To the extent that the tax loss carryforward is realized in the future, such deferred credit will be reinstated at the tax rates then in effect. A cumulative deferred tax charge of \$38,300 which arose in prior years was written off in 1976, because future realization was not assured. In the event that expense to which such deferred tax charge relates is applied in

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

reducing future taxable income, the tax effect thereof will be recorded as extraordinary income at that time.

At December 31, 1981, Industries and its subsidiaries had a net operating loss carryforward for financial statement purposes of approximately \$459,000, and a capital loss carryforward of approximately \$460,000. For financial statement purposes the tax benefit from such carryforward will be recorded as extraordinary income to the extent that future earnings are generated within the loss carryforward period in excess of the amounts required to restore deferred tax credits.

At December 31, 1981, Industries and its subsidiaries have a tax loss carryforward of approximately \$538,000 of which \$110,000 expires in 1994 and \$417,000 expires in 1995. In 1980 the Internal Revenue Service completed its examinations of Industries' Federal income tax returns for the years 1975 through 1977. No additional tax other than that previously provided for was assessed. Industries' net operating loss carryforward may be reduced upon the sale of the stock of SLC.

(9) Common Stock

In 1979, stockholders approved the grant of non-qualified stock options to purchase 50,000 shares of common stock to each of Messrs. Ralph T. McElvenny, Jr., Chairman of the Board, and Brian P. Burns, Chairman of the Executive Committee, at a price of \$2.50 per share (\$250,000 in the aggregate) exercisable at any time in whole or in part through April, 1986. The closing price of Industries' common stock as traded on the American Stock Exchange as of the date of the grant was \$2.63 per share (\$263,000 in the aggregate). As of December 31, 1981 such options had not been exercised.

Industries has adopted a program to make repurchases of its common stock. Under the program, from time to time Industries may repurchase a total of up to 75,000 shares in the open market or privately at prices deemed attractive. As of December 31, 1981 2,600 shares have been purchased at an average price of \$2.00 per share.

(10) Information on Segments of Business, Exports and Major Customers

Industries' significant business segments are presented below.

Lighting Products. The lighting products subsidiary manufactures lighted and unlighted instrument panels and dials, primarily for aerospace and electronic application.

Metal Products. The metal products subsidiary primarily supplies precision marked dials and other components for watches, aerospace and electronic applications, and unlighted and self-luminous dials for watches, clocks and timers for consumer and automotive applications.

Financial data respecting the above Industry segments, exports and major customers in 1981, 1980 and 1979 are as follows (in thousands):

	Year ended December 31		
	1981	1980	1979
Net sales and other income			
Lighting Products	\$2,422	2,060	1,478
Metal Products	959	980	1,287
Other Income	235	149	96
	<u>\$3,616</u>	<u>3,189</u>	<u>2,861</u>
Earnings (loss) from continuing operations before income taxes, allocated administration expense and extraordinary items			
Lighting Products	\$ 642	451	282
Metal Products	60	28	125
Corporate Expense	(1,004)	(1,076)	(1,007)
Other Income	235	149	96
Interest Expense	(19)	(7)	(31)
	<u>\$ (86)</u>	<u>(455)</u>	<u>(535)</u>
Identifiable assets			
Lighting Products	\$1,072	951	690
Metal Products	400	449	540
Discontinued operations	281	3,426	3,787
Corporate (principally cash, investments and office facilities)	4,444	1,979	2,316
	<u>\$6,197</u>	<u>6,805</u>	<u>7,333</u>

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Information on Segments of Business, Exports and Major Customers (Cont'd)

	Year Ended December 31		
	1981	1980	1979
Depreciation and amortization			
Lighting Products	\$ 39	23	22
Metal Products	45	50	52
Discontinued operations	103	185	189
Corporate	15	14	19
	<u>\$ 202</u>	<u>272</u>	<u>282</u>
Capital expenditures			
Lighting Products	\$ 16	171	12
Metal Products	3	2	20
Discontinued operations	48	78	163
Corporate	14	13	5
	<u>\$ 79</u>	<u>264</u>	<u>200</u>

In 1981 Industries largest customer accounted for 14% of total revenue. In 1980 no one customer's sales accounted for 10% or more total revenue. In 1979 Industries largest customer accounted for 15% of total revenue.

(11) Leases

Industries' plant facilities are leased under non-cancellable leases, the initial terms of which will expire at various times during the next three years. Management anticipates that in the normal course of business, such leases will be extended or replaced by other leases.

Operating Leases. Lighting has a production facility under an operating lease which provides for minimum lease payments of approximately \$50,000 annually through 1983.

Total rent expense charged to operations, which includes the above operating lease, during the years ended December 31, 1981, 1980 and 1979 was \$63,220, \$53,588 and \$54,544 respectively.

(12) Other Investments

(a) During 1980, Industries executed a commitment agreement with Traverse Oil Company ("Traverse") Traverse City, Michigan, pursuant to which Industries committed to participate with Traverse in drilling test wells under Traverse's 1980 oil and gas exploration program at an estimated cost to Industries of \$200,000. Joseph G. Kozrzewa, a Director of Industries, is Presi-

dent and a Director of Traverse. As of December 31, 1981, Industries had paid or accrued liabilities under its commitment with Traverse totaling approximately \$144,000 of which \$132,000 applicable to dry holes was charged to operations.

Because of Industries' operating losses, the economics of exploration drilling became less favorable to Industries than at the date when the commitment was executed, at which point it was expected that Industries would generate taxable earnings for 1981. Accordingly, Industries' Board of Directors sought relief from ongoing financial responsibility under the drilling commitment and authorized Messrs. Brian P. Burns, a Director of Industries, and Ralph T. McElvenny, Jr., Chairman of Industries, together with certain unrelated persons who were financially qualified and acceptable to Traverse, to assume Industries' ongoing financial responsibility subsequent to March 13, 1981. All such rights and liabilities were assumed on the same terms and conditions as under Industries' original commitment agreement of 1980. The approximate aggregate amount of all costs and expenses assumed for the period after March 13, 1981 is estimated as not less than \$125,000.

(b) During March, 1981 Industries reached agreement with Titan Wells, Inc. ("Titan") to purchase from Titan warrants exchangeable on a one-for-one basis into 250,000 shares of voting common stock of Titan at a price, subject to certain conditions, of \$2.00 per warrant, totalling \$500,000. Mr. Ralph T. McElvenny, Jr., is Chairman of the Board and a controlling stockholder of Titan. Titan owns directly at December 31, 1981, 293,603 shares of common stock of Industries, constituting approximately 25% of the total shares outstanding. In view of changes in general market conditions and of the time required by Titan to complete additional warrant sales to third parties having no equity ownership in Titan as of January 1, 1981, which sales had been required by Industries as a condition to its investment, during December, 1981 the parties modified their agreement and adjusted the purchase price to \$1.20 per warrant. At the more favorable price as adjusted, Industries' warrants are exchangeable into 416,667 Titan shares constituting approximately 15% of the total of Titan's common stock outstanding. The warrant contract bears no expiration date but may be rescinded by Industries unless Titan receives paid subscriptions to purchase at least 150,000 shares of its common stock at price of not less than \$1.35 per share and the issuance of the underlying Titan shares shall have been authorized by Titan shareholders as of June 30, 1982. Mr. McElvenny has agreed to vote all of the Titan stock beneficially owned by him in favor of a proposal to appropriately increase Titan's

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

number of authorized shares. Titan is a public company which files with the Securities and Exchange Commission, under Commission File Number 0-4132, reports required under the Securities and Exchange Act of 1934.

(c) At the Annual Meeting of Stockholders of USRC held May 16, 1979, a proposal to purchase interests in certain income producing oil and gas wells and exploration acreage owned by Titan Wells, Inc., on terms approved by the Board of Directors, was ratified and approved by stockholders. In connection with such transactions, USRC issued to Titan 50,000 restricted and unregistered shares of USRC common stock, valued at \$2.50 per share, and assumed \$43,795 principal amount of bank indebtedness of Titan.

(d) During 1981 Industries established a stock ownership in Boothe Financial Corporation ("BFC"), a San Francisco, California based company engaged in diversified real estate and financial services. At present, Industries owns directly 72,000 shares of BFC or slightly less than five percent of BFC's total shares outstanding, for which Industries paid an average price of \$25.22 per share inclusive of commission charges for a total of \$1,816,000. During September, 1981 Mr. Brian P. Burns, a San Francisco attorney who is a Director and Chairman of the Executive Committee of Industries and who has been a Director of BFC since 1976, was named Chairman of the Board and Chief Executive Officer of BFC. Also, Mr. Ralph T. McElvenny, Jr., Chairman of the Board of Industries, was named a Director and member of the Executive Committee of BFC.

(e) A summary of investments carried at the lower of cost or market is as follows at December 31, 1981 and 1980:

Names of Issues	1981	1980
First of Denver Mortgage Investors	\$ —	146,250
Boothe Financial Corporation	1,656,000	—
Titan Wells, Inc.	500,000	—
Oil and gas working interests	163,154	205,010
Total	<u>\$2,319,154</u>	<u>351,260</u>

(13) Legal Proceedings

(a) On May 9, 1980 SLC, the corporate successor to USRC, initiated action in Superior Court, Morris County, New Jersey, against Penteco, a California partnership and SLC's former distributor of certain commercial self-illuminating emergency signs, seeking, inter alia, judicial declaration that because of Penteco's conduct SLC was justified in terminating Penteco as its distributor. This action has been stayed pending the outcome of the California litigation described below.

In a separate action filed by Penteco against USRC on May 9, 1980 in U.S. District Court, Central District of California, Penteco has asserted claims against SLC for lost profits and other damages due to the alleged breach of such contract by SLC, which purportedly may exceed \$750,000 and added claims for treble damages under the Sherman and Clayton Acts for purported anti-trust violations by SLC in connection with termination of such contract. SLC has asserted several counter-claims in the California action, including claims for breach of contract, for goods sold and delivered at Penteco's request and for tortious interference by Penteco with the SLC's contractual relationships.

SLC has been advised by counsel that it has meritorious defenses to the allegations by Penteco. At present, because the litigation is in its pretrial stages, the outcome is difficult to predict; however, management intends to vigorously contest this litigation and, based on its current knowledge as to the allegations by plaintiff, believes that the ultimate possibility of material recovery by plaintiff is unlikely.

(b) In February, 1981 a copy of a civil complaint was received which had been filed in January, 1981 in the U.S. District Court for the Southern District of Indiana by an individual plaintiff on her own behalf and as administratrix of her late husband's estate, naming USRC, five other named persons and various unnamed persons as defendants. The complaint alleged personal injury and wrongful death of plaintiff's decedent for alleged injury in handling radioactive materials and sought damages in unspecified amount to be proven at trial and punitive damages of one million dollars.

On August 7, 1981 plaintiff's action was dismissed. Plaintiff received no payment or other recovery whatsoever against USRC.

(c) On April 2, 1981 an action was commenced in Superior Court of New Jersey by one T & E Industries, Inc. against USRC and alleging, inter alia, that property owned in Orange, New Jersey suffers from contamination from certain radioactive materials deposited thereon by USRC during prior years. The plaintiff seeks damages in unspecified amount to be proven at trial in compensation for injury to its property and business. The litigation, which is in its early stages, appears to arise from operations conducted by USRC at some time or times during the period from 1917 to World War II in 1943. While it is too early for counsel to form an opinion as to the probable outcome, management intends to vigorously contest this litigation and, based on its current knowledge as to the allegations by plaintiff, believes that the ultimate possibility of material recovery by plaintiff is unlikely.

ACCOUNTANT'S REPORT

The Board of Directors and Stockholders

USR Industries, Inc.:

We have examined the consolidated balance sheets of USR Industries, Inc. and subsidiaries as of December 31, 1981 and 1980 and the related consolidated statements of operations, stockholders' equity, and changes in financial position for each of the years in the three-year period ended December 31, 1981. Our examinations were made in accordance with generally accepted auditing standards, and accordingly included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, the aforementioned consolidated financial statements present fairly the financial position of USR Industries, Inc. and subsidiaries at December 31, 1981 and 1980 and the results of their operations and the changes in their financial position for each of the years in the three-year period ended December 31, 1981, in conformity with generally accepted accounting principles applied on a consistent basis.

Short Hills, New Jersey
March 17, 1982

Per: Manning H. H. H.

USR INDUSTRIES, INC. AND SUBSIDIARIES

FINANCIAL REVIEW SELECTED FINANCIAL DATA

(The five years of selected financial data are not covered by Accountants' Report)

(In thousands except per share amounts)

	Year Ended December 31				
	1981	1980	1979	1978	1977
Total revenues	\$3,616	3,189	2,861	3,227	2,927
Loss from continuing operations before extraordinary items	\$ (86)	(358)	(535)	(625)	(397)
Loss per share from continuing operations before extraordinary items	\$ (.08)	(.31)	(.46)	(.56)	(.36)
At year-end Total assets	\$6,197	6,805	7,333	6,061	7,026
Long term obligation	\$ 66	67	67	93	117

No cash dividends have been declared of the above in any years.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Liquidity and Capital Resources

Industries and its subsidiaries depend upon internally generated earnings to furnish adequate capital to finance their activities.

During 1981 many customers of Metals and Lighting, especially in automotive and watch makers, were forced to adjust inventories, manufacturing procedures and levels of general business activity in response to competition from overseas imports, poor economic conditions in the United States, inflationary trends and other factors.

At year end working capital had decreased by \$1.2 million compared to December 31, 1980, while the ratio of current assets to current liabilities decreased from 4.3:1 at December 31, 1980 to 3.6:1 at December 31, 1981. Industries' stated liquidity position diminished due primarily to the sale of Chemicals, the proceeds of which were used to purchase shares of common stock of Boothe Financial Corporation ("BFC") which are classified in the accompanying statements as a non-current asset. To fund its internal cash needs Industries relied primarily on reduction of accounts receivable and other current accounts. Except as required in the ordinary course of business, Industries has no plans to make material additional capital expenditures in the near future.

Trend

Metals and Lighting are attempting to adjust operations to respond to adverse economic conditions and changing patterns of consumer preference. In view of Industries' record of performance over several years there can be no assurance that, if required, external debt or equity could be obtained either privately or in the public capital markets. In response to what it believes are adverse trends in its continuing business sectors, the availability of better opportunities for growth and potential appreciation in other sectors and other factors, Industries is actively considering alternative methods of redeploying its assets, including sale of assets and other restructuring, pursuant to its program of asset redeployment.

During 1981 Industries established an ownership position in the common stock of BFC, a San Francisco, California based company engaged in diversified real estate and financial services. Industries owns directly 72,000 shares of BFC or slightly less than five percent of BFC's total shares outstanding, for which Industries paid an average price of \$25.22 per share inclusive of commission charges, for a total of \$1,816,000. BFC is believed to be an attractive investment for Industries, primarily because (1) it is engaged in economic sectors—real estate and financial services—previously identified by management as potential growth areas and (2) BFC enjoys a liquid financial position, having reported cash and cash-equivalent holdings as of September 30, 1981 totaling \$42,658,000, or approximately \$26.64 per share of BFC common stock outstanding as of that date. During September 1981, Mr. Brian P. Burns, a San Francisco attorney who is a Director and Chairman of the Executive Committee of Industries and who has been a Director of BFC since 1976, was named Chairman of the Board and Chief Executive Officer of BFC. Also, Mr. Ralph T. McElvenny, Jr., Chairman of the Board and President of Industries, was named a Director and member of the Executive Committee of BFC.

Inflation and Changes in Prices

Industries continues to experience pressure from customers to reduce prices or reduce the rate of price increases in all of its business segments. The policy of Industries is to resist such pressure insofar as possible and to attempt to pass on inflationary cost increases through price increases. Management can offer no assurance that inflationary cost increases affecting Industries' manufacturing operations can be recovered through price increases, internal efficiencies or otherwise.

1981 Compared with 1980

During 1981 net sales totaled \$3.4 million compared to \$3.0 million during 1980. The sales increase is due

primarily to the completion of orders which were in inventory and backlog at December 31, 1980, and the high rate of production by Lighting during the first half of 1981. New orders declined by approximately 20% compared to 1980 and sales during the second half of 1981 were lower than the first half because of the decline in new orders.

Other income increased by \$87 thousand during 1981 due to increased income from short term investments and dividend income from investments in securities.

Cost of sales increased from \$2.4 million during 1980 to \$2.6 million during 1981, due primarily to increased sales volume. As a percent of product sales, cost of sales decreased from 78.8% during 1980 to 75.6% during 1981.

Selling, administration, and general expenses decreased from \$1.2 million during 1980 to \$1.1 million during 1981, due primarily to reduced data processing costs and elimination of costs related to a centralized administrative building utilized during most of 1980 but subleased in 1981. These cost savings were somewhat offset by increased legal and professional fees.

There is no income tax benefit during 1981 compared to a tax benefit of \$97 thousand during 1980.

As a result of the above, loss from continuing operations before extraordinary item decreased from \$358 thousand during 1980 to \$86 thousand during 1981.

Earnings from operations of discontinued businesses increased from \$12 thousand during 1980 to \$44 thousand during 1981 due primarily to improved performance of Chemicals during 1981; however, this increase was offset during 1981 by a loss of \$385 thousand on the disposal of discontinued businesses.

After including effect of the operations and disposal of discontinued businesses the net loss for Industries decreased from \$336 thousand during 1980 to \$322 thousand during 1981.

1980 Compared with 1979

During 1980 net sales totaled \$3.0 million compared to \$2.8 million during 1979. Lighting's sales increased by approximately \$582 thousand; however, this increase was partially offset by a \$307 thousand decrease in Metals' sales.

Other income increased by \$53 thousand during 1980 due to increased income from investments, including gain on sale of marketable securities and short term investments on the net income of Unatco Funding Corporation.

Cost of sales increased from \$2.2 million during 1979 to \$2.4 million during 1980 due primarily to increased sales volume.

Interest expense decreased from \$31 thousand during 1979 to \$7 thousand during 1980, due primarily to provision for increased interest expenses for adjustments proposed by the Internal Revenue Service.

There was no tax benefit during 1979 compared to a tax benefit of \$97 thousand during 1980. The tax benefit of \$97 thousand primarily pertains to elimination of deferred tax credits.

Earnings from operations of discontinued businesses decreased from \$734 thousand during 1979 to \$12 thousand during 1980. This decrease was due primarily to volume decline at Chemicals following completion in 1979 of higher than normal demand for start-up requirements of a European customer.

There was an extraordinary credit of \$492 thousand during 1979, to reflect the tax benefit from a net operating loss carryforward after reinstatement of deferred tax credit written off in prior years.

Net earnings were \$691 thousand during 1979 compared to a loss of \$336 thousand during 1980.

1979 Compared with 1978

During 1979 net sales totaled \$2.8 million compared to \$3.2 million during 1978. Metals' sales declined \$622 thousand reflecting lower volume of dials for watches and precision marking of crystals for watches. Sales by Lighting increased \$184 thousand over the prior year.

Other income increased \$72 thousand in 1979 due primarily to increased income from investments, including the oil and gas interests purchased from Titan Wells, Inc. on terms as approved by stockholders on May 16, 1979 and net income of Unatco Funding Corporation.

Cost of sales decreased from \$2.9 million during 1978 to \$2.2 million during 1979, due primarily to decreased sales volume.

Selling, administration and general expenses increased \$264 thousand in 1979, principally because of general inflation, increased legal and consulting fees, and for incentive compensation and bonuses. Such increases were partially offset by decreased marketing expenses during 1979.

Earnings from operations of discontinued businesses increased from a loss of \$156 thousand in 1978 to a profit of \$734 thousand in 1979, due primarily to increased vol-

1982
Annual
Report

ume of Chemicals based on the acceptance of new phosphors and higher than normal requirements for customer start up using the new products.

In 1979 an extraordinary credit of \$492 thousand reflects the tax benefit of a net operating loss carryforward after reinstatement of deferred tax credits written off in prior years.

Net earnings were \$691 thousand in 1979 compared to a loss of \$781 thousand in 1978.

General Development of Business

The financial statements for 1979 relate to United States Radium Corporation ("USRC"). Pursuant to an Agreement and Plan of Merger dated May 16, 1980 and approved by shareholders of USRC, on August 27, 1980 a newly formed subsidiary of Industries was merged into USRC on a basis whereby shares of common stock of USRC were deemed to have been converted share for share into shares of common stock of Industries.

On June 15, 1981 Industries sold certain assets owned by or used in the business of its chemical products subsidiary, USR Chemical Products, Inc., ("Chemicals") to Mitsubishi Chemical Industries Ltd., a Japanese corporation, for a purchase price of approximately \$2.4 million. The assets of Chemicals retained by Industries have been reclassified in the accompanying balance sheets as net current and non-current assets of discontinued businesses.

Pursuant to a plan adopted on December 15, 1981, Industries plans to sell the stock of its wholly owned subsidiary Safety Light Corporation ("SLC"), and certain assets of USR Metals, Inc. ("Metals") to a group led by current executive officers of SLC. The transaction is expected to be completed during 1982. In the accompanying balance sheet such net assets held by Industries for disposal have been reclassified as net current and non-current assets of discontinued businesses.

Narrative Description of Business

During 1982 Industries intends to establish the operations described below as subsidiaries of a newly formed common parent corporation and to recognize the closely related nature of their respective product lines by consolidating the operating reports thereof.

Metal Products. USR Metals, Inc. ("Metals") supplies marked dials and other components for watches, aerospace and electronic applications, and unlighted and self-luminous dials for watches, clocks and timers for consumer and automotive applications. Metals markets directly to industrial customers through technical personnel, executives and independent sales representatives. Generally, these products are engineered and sold on a quoted fixed-price basis.

Lighting products. USR Lighting, Inc. ("Lighting") manufactures lighted and unlighted instrument panels and dials, primarily for aerospace and electronics applications. Lighting markets directly to customers through technical personnel, executives and independent sales representatives. Products are engineered and manufactured to specific customer specifications and are generally quoted on a fixed-price basis. Lighting is dependent upon sales to a limited number of customers, the loss of any one or more of which would have an adverse effect upon Lighting and Industries.

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MARKET PRICE OF THE REGISTRANT'S COMMON STOCK AND RELATED SECURITY HOLDER MATTERS

Principal Market and Stock Prices

Principal market on which Industries' common stock is traded:

American Stock Exchange

The table below presents the high and low market prices and dividend information for Industries' common stock:

	<u>High</u>	<u>Low</u>
<u>1981</u>		
First Quarter	\$3¾	\$2½
Second Quarter	3¾	2½
Third Quarter	3	1¾
Fourth Quarter	2½	1¾
<u>1980</u>		
First Quarter	5¼	2¾
Second Quarter	3½	2½
Third Quarter	4¾	2¾
Fourth Quarter	\$3¾	\$2½

Approximate Number of Holders of Common Stock

At March 15, 1982, the number of holders of record of each class of Industries' equity securities was as follows:

<u>Title of Class</u>	<u>Number of Record Holders</u>
Common stock	
\$1 par value	1,650

Dividend Information

No cash dividends were declared or paid during the above two year period. Management of Industries does not believe it likely that Industries will pay any cash dividend in the foreseeable future.

ANNUAL REPORT ON FORM 10-K

The Annual Report to the Securities and Exchange Commission on Form 10-K is available to stockholders of record without charge upon written request to the Corporation at 2203 Timberloch Place, Suite 216A, The Woodlands, Texas 77380.

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